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**REPORT BY THE EXTERNAL AUDITOR ON THE PERFORMANCE AUDITS
UNDERTAKEN IN THE 2004-2005 BIENNIUM**

**Draft action plan proposed by the Director-General
on management of extrabudgetary funds**

SUMMARY

In the performance audits undertaken by the External Auditor during the 2002-2003 and 2004-2005 biennia on management of UNESCO's extrabudgetary funds (169 EX/29 and 174 EX/27), a number of perceived weaknesses have been identified with regard to the strategies and procedures for the programming, resource mobilization, implementation and monitoring of extrabudgetary activities, and a series of recommendations have been made. Based on the findings of an internal working group established to this effect, and following discussions among UNESCO's senior management, the Director-General has approved a series of proposals for an action plan in response to the critique and recommendations of the External Auditor. As stipulated in paragraph 83 of document 174 EX/26, the Director-General is submitting in this document the main orientations of these proposals for the information of the Executive Board. Based on the observations of the Board, and following a series of subsequent consultations with all major stakeholders, the Director-General intends to submit finalized proposals to the 175th session of the Executive Board.

INTRODUCTION

1. During the 2002-2003 and 2004-2005 biennia, the performance audits undertaken by the External Auditor have in major part been devoted to the management of UNESCO's extrabudgetary funds, which in recent years have come to constitute more than half of the resources available to the Organization. The first report in this respect (169 EX/29) focused on the overall management of extrabudgetary funds, reviewing in particular the roles and responsibilities with regard to the programming, resource mobilization, implementation and monitoring of extrabudgetary activities. The second report (174 EX/26) is based on a series of field studies of the planning and implementation of individual extrabudgetary projects.

2. Both reports from the External Auditor have identified a number of perceived weaknesses regarding UNESCO's strategies and procedures for the management of extrabudgetary funds, and made a number of recommendations for improvement. The recommendations have first and foremost called for a more strategic and consistent programming of extrabudgetary activities, aligned with the principal priorities of UNESCO's major programmes, responding to the needs of the beneficiary countries, and respecting the priorities of the funding sources. The External Auditor has also pointed to the need to coordinate more effectively, through a clear distribution of responsibilities, UNESCO's mobilization of extrabudgetary funds in reflection of the priority programmes identified. Furthermore, the External Auditor has underlined the necessity of more effective measures to ensure timely and adequate implementation of extrabudgetary activities, implying regular analysis of delivery rates, and pertinent remedial action. Finally, the Auditor has recommended measures and tools, notably timely summary reports, to enhance the monitoring by UNESCO's senior management, and by the governing bodies, of UNESCO's delivery of extrabudgetary activities. In light of this, the External Auditor has invited the Director-General to develop an action plan to improve the management of extrabudgetary funds.

3. While the Director-General has deployed major efforts to implement the recommendations of the External Auditors, and has provided regular reporting to the Executive Board to this effect, it is recognized that further improvement is needed to ensure optimal programming and utilization of extrabudgetary funds in direct reinforcement of the main priorities identified in UNESCO's regular programme and budget, and the Medium-Term Strategy. In March 2005, the Director-General therefore created an ad hoc working group on extrabudgetary activities, comprising representatives for the Programme Sectors and the most concerned central services. Based on the findings of the working group, discussions took place within the College of ADGs in November 2005 and February 2006, leading to the identification of a series of proposals to enhance UNESCO's overall policies and processes in the field of management of extrabudgetary activities, and also describing the tools that exist, or need to be developed, to support the major process steps. These proposals have been approved by the Director-General.

4. Below are outlined the overall orientations of the proposals, responding to the various recommendations by the External Auditor relating to the main stages of management of extrabudgetary funds:

- programming;
- resource mobilization;
- implementation;
- monitoring.

5. In the light of the observations of the Executive Board, and following a series of subsequent consultations with all major stakeholders, the Director-General intends to submit finalized proposals to the 175th session of the Executive Board.

PROGRAMMING OF EXTRABUDGETARY ACTIVITIES

Background and guiding principles

6. Since the inception of document 31 C/4, UNESCO's extrabudgetary contributions have been regarded as an integral part of the Organization's overall resource base. Regular programme and extrabudgetary activities must therefore be planned together with a view to be mutually reinforcing; and this principle is embedded in UNESCO's current programme management cycle. The definition of the Sector Strategic Frameworks (SSFs) for document 33 C/5 therefore also comprised projected extrabudgetary activities; and the Programme Review Committees (PRCs) are meant to review such activities as well. However, in spite of efforts in this regard, it must be recognized that the 33 C/5 planning process did not succeed in fully integrating projected extrabudgetary activities in UNESCO's overall activity plan. Furthermore, and more importantly, there has been virtually no linkage in practice between the planning process, and subsequent presentation by the programme sectors and the field offices of activities to be financed from extrabudgetary sources. The operational solutions identified below reflect the following guiding principles:

- Extrabudgetary activities must be planned in the context of the preparation of the C/5 documents; and there must be a “seamless” linkage between the two sets of activities;
- The definition of the SSFs, and the subsequent discussions in the sector/regional PRCs, must reflect UNESCO's overall strategies and visions, but must also take sufficiently into account the “bottom-up” approach as represented by the contributions from the field offices in reflection of broadly approved national development strategies. An enhanced UNESCO participation in country level programming exercises such as the United Nations Development Assistance Frameworks (UNDAFs) and Poverty Reduction Strategies (PRSs) will be important factors in this process, as will the preparation of an increasing number of UNESCO country programming documents;
- The “up-front” planning of projected extrabudgetary activities, in the context of the preparation of the C/5 document, will remain the overall guide for UNESCO's relations with extrabudgetary funding sources throughout the biennium. However, the planning process must allow for regular updates and adjustments to evolving needs of Member States, so that these needs may be met from extrabudgetary contributions as is currently the case.

Policy decision and implementation processes

7. **Policy decision:** In the context of the elaboration of the draft C/5 document, “extended” (extrabudgetary) sectoral strategic frameworks will also be elaborated, so that the SSFs cover both regular budget and projected EXB activities. The SSFs will include specific objectives for EXB resource mobilization, and results to be attained. Through the meeting of the “unfunded needs” thus identified, EXB activities will in particular be targeted at activities at country level that enhance the regular budget activities, thus allowing UNESCO's action to reach the defined overall results, and have greater impact.

8. **Implementation processes:**

- In the context of the elaboration of the SSFs for the regular budget, the projected EXB activities are developed by the sector ADGs, in close consultation with the relevant field offices (FOs) and (category 1) institutes, and also reflecting the cluster strategic frameworks. An indicative ratio between the level of regular budget and desired extrabudgetary resources is defined.
- Upon approval by the Director-General, the “extended” SSFs are translated into EXB programme outlines to be included in “an additional programme” of projected/targeted EXB activities, preferably at a detailed level which corresponds to the MLAs in the C/5 document.
- The programme outlines to be included in the “additional programme” are assessed by separate sector/regional review committees (also comprising the Bureau for Strategic Planning (BSP) and the Division for Cooperation with Extrabudgetary Funding Sources (ERC/CFS), based on a predefined set of criteria (overall quality of the programme, relevance to UNESCO’s mandate and the country planning process, UNESCO’s delivery capacity, comparative advantage, and value added, as well as the longer-term sustainability of the programme), and taking account of available information on the policies and priorities of the funding sources. The programme sector ADGs play the key role in this prior quality control.
- The selected project outlines are included in the UNESCO “additional programme” in the form of a project/programme pipeline, and serve as basis for a proactive resource mobilization strategy. Broad collective consultations with the funding sources on these “unfunded needs” are undertaken (possibly in the margin of the General Conference) under the overall leadership of ERC/CFS to allow indications of general interest for one or several of the programmes seeking extrabudgetary funding.
- Upon interest shown by donors for a programme outline contained in the “additional programme” it would be seen with the donor in question whether more detailed programme/project documents would have to be developed for approval, or whether simple work plans for allotment and monitoring purposes would suffice.
- Prior to the formal presentation to the funding sources (and prior to undertaking any commitment on behalf of UNESCO), the budget associated with the project outline/document must obtain the visa of the Bureau of the Budget (BB), ensuring compliance with UNESCO’s budget standards, as well as with the Organization’s cost recovery policies, including programme support costs, implying that all costs associated with extrabudgetary activities must be recovered from the funding source.

EXTRABUDGETARY RESOURCE MOBILIZATION

Background and guiding principles

9. In the absence of overall strategies for UNESCO’s programming of extrabudgetary activities, resource mobilization strategies are not systematically formulated and applied at present. While UNESCO, through the current ad hoc approach, has been quite successful in mobilizing large amounts of extrabudgetary funding for the Organization’s activities, this approach needs to be reconsidered in view of UNESCO’s increased dependence on extrabudgetary contributions. Failure

to ensure an overall strategic framework for resource mobilization, and an effective coordination of contacts with potential donors, may lead to dissensions and wasted efforts, and may eventually tarnish UNESCO's image. The operational solutions identified below reflect the following guiding principles:

- The basis for UNESCO's extrabudgetary resource mobilization strategy is the above described "additional programme" in direct extension of the C/5 documents, reflecting both UNESCO's overall strategic visions and contributions flowing from relevant country programming exercises, and also taking into account the policies and priorities of the funding sources;
- Extrabudgetary resource mobilization is a joint responsibility of the programme sectors, field offices, institutes and ERC/CFS; but adequate coordination must be ensured by ERC/CFS through a consistent exchange of information. All formal presentations to funding sources of programme/project outlines/proposals should preferably take place through ERC/CFS on condition that modalities be identified to ensure that this would not represent an administrative bottleneck;
- The specific role of the field offices in resource mobilization from field oriented multilateral funding sources – mainly the European Commission, the multilateral development banks, and the United Nations funds and programmes – will be further developed through targeted training, and more effective modalities for exchange of information with ERC/CFS.

Policy decision and implementation processes

10. **Policy decision:** UNESCO has a unified resource mobilization strategy and donor approach, based on the "UNESCO extended SSFs" (also including the introductions to each major programme of document C/5), and the EXB resource mobilization strategic plan, developed and implemented under the overall coordination of ERC/CFS in consultation with BSP, programme sector ADGs, field offices and institutes, and based on information on the policies and priorities of the funding sources.

11. Implementation processes:

- In parallel with the elaboration of the extended SSFs, ERC/CFS develops an "EXB mobilization strategic plan", drawing, through a continued dialogue process, on information available from the donors themselves, as well as from programme sectors, field offices and institutes. This plan will serve as the basis for the implementation of all resource mobilization activities in terms of distribution of labour, and modalities/mechanisms for approaching the funding sources.
- In the development of the strategic plan, ERC takes account of the results of the "collective donor consultations" that will be organized in the margin of each General Conference. A calendar of subsequent collective or individual donor events will also be established.
- Delegated authority with respect to decentralized resource mobilization is maintained, with the main emphasis on decentralized funding sources, notably multilateral sources.

- The scope for innovative funding modalities, notably of a multi-donor multi-year nature, with little or no earmarking, will be further explored, as will perspectives for a further diversification of UNESCO's funding sources.
- UNESCO's formats and modalities for funding agreements, and plans of operations, will be reviewed for continued adequacy.

ISSUES RELATING TO PROJECT/PROGRAMME IMPLEMENTATION

Background and guiding principles

12. It is the general view that current rules and procedures relating to actual project and programme implementation – i.e. the phase beginning with the creation of the project by BB, and the transfer of the funds by the funding source, and terminating with the formal closure of the project account – by and large are adequate (albeit in some cases cumbersome), but insufficiently adhered to by staff. More consistent monitoring at senior management level is therefore necessary.

13. A number of the problems currently weighing on UNESCO's implementation of extrabudgetary activities – frequently implying both quantitative and qualitative insufficiency in actual delivery – are likely to be mitigated through better programming of the activities, notably in terms of prior quality control, and assurance of UNESCO's delivery capacity. Nevertheless, a number of measures must be taken also in the short term to improve UNESCO's implementation and monitoring of extrabudgetary activities. The operational solutions identified below reflect the following guiding principles:

- **Substantive monitoring and narrative** reporting regarding extrabudgetary activities must be given higher priority, both in response to the expectations of the donors and the beneficiaries, but notably as UNESCO's own tool to monitor developments, and take remedial action as necessary. UNESCO's standard formats for narrative reporting must be respected, as must the timeline for the preparation and distribution of the reports, based on an effective centralized monitoring system. Sufficient quality control must be exercised by the programme ADGs/Directors of field offices. Regular reviews must be carried out by the project manager of the continued adequacy of the project design; and modifications proposed to the funding source and the beneficiary as necessary;
- **Financial monitoring and reporting** must be improved, and adequate financial reports presented in a more comprehensive, timely and user-friendly manner. Since quantitative disbursement reports do not provide the full picture of the (in)adequate implementation of a project/programme, the reports must reflect the relationship between the funds received, allocations and disbursements, and the activities implemented. At least once a year, the budget and payment schedule must be reviewed, and revisions proposed as necessary. Existing provisions to ensure a timely closure of the project account after termination of the project must be respected;
- **Evaluations**, whether mid-term or final, of all major and/or innovative projects/programmes must be ensured, implying that the original project design must lend itself to such evaluation, and that the budget must contain adequate financial provisions. A central database must be established to keep track of all major lessons learned; and project managers must consistently consult the database when preparing new proposals in the same field.

SUBSTANTIVE MONITORING AND NARRATIVE REPORTING

Policy decision and implementation processes

14. **Policy decision:** In line with the unified EXB resource mobilization strategy, and the unified approach to funding sources, UNESCO equally has a unified substantive monitoring and reporting approach in terms of basic content and periodicity. This approach will be based on standard reporting formats reflecting the results-based management framework, and previously agreed with the main funding sources. It will also ensure adherence to the timeline for the preparation and distribution of the narrative, including final reports.

15. Implementation processes:

- Standard formats for progress and final reporting, based on the results-based management framework, will be developed, and prior agreement with the funding sources on the format and the periodicity of the narrative reporting will be sought.
- Systematic review, as part of the monitoring and resulting narrative reporting, will take place of possible needs for revising the project design, and the consequent need to obtain the approval of the funding source (and beneficiary).
- A quality review mechanism will be developed at Headquarters to review narrative reports prior to the sending to the donors and beneficiaries, and subsequent posting on UNESCO's website, should the main stakeholders so agree.

FINANCIAL MONITORING AND REPORTING

Policy decision and implementation processes

16. **Policy decision:** In line with the unified EXB resource mobilization strategy, and unified approach to funding sources, UNESCO equally has a unified financial monitoring and reporting approach in terms of basic content and periodicity. This approach is based on activity reporting (as an expansion of the normal budget line reporting), as well as on prior agreement with the funding source on periodicity (normally annual end-year reports), as well as a final financial report.

17. Implementation processes:

- Standards and minimal formats for financial reports will be developed, also taking into account possible specific requirements of the funding sources.
- The standard funding agreement will be adapted to account for exchange rate variations, and to include the payment schedule.
- Systematic reviews, as part of the financial reporting, will be carried out of possible needs to modify the budget, with the consequent need to obtain the approval of the funding source. Annual budget revisions must be considered as a minimum.
- Systematic monitoring will take place (by the administrative officers (AOs), the Division of the Comptroller (DCO) and BB) after operational termination of a project of the disbursement of final payments, liquidation of outstanding obligations, and notification to ERC/CFS of possible savings/deficits that need to be settled with the funding source with a view to ensuring subsequent timely closure of the project account.

EVALUATION

Policy decision and implementation processes

18. **Policy decision:** UNESCO will apply a systematic approach to ensure appropriate mid-term and final evaluations of all major (or innovative) extrabudgetary activities.

19. **Implementation processes:**

- Standard formats for terms-of-reference for mid-term and final evaluations will be developed, reflecting the results based management framework of the project design, and will be included in the project/programme document, and agreed in principle with the funding source at the inception of the activity. The requisite funds will be included in the approved budget.
- Timely invitations will be extended to the funding source for comments on the terms-of-reference, and for participation on the evaluation itself.
- A database will be developed to summarize all major findings of evaluations of extrabudgetary activities, as well as their relationship with similar regular programme activities. Systematic recourse to this data base will be ensured during the preparation of proposals for future similar activities.

TOOLS FOR MONITORING OF EXTRABUDGETARY ACTIVITIES BY SENIOR MANAGEMENT, AND UNESCO'S GOVERNING BODIES

20. **Background and guiding principles**

There is general agreement that UNESCO's senior management – the programme sector ADGs, the directors of field offices, the College of ADGs, and the Directorate – needs to be more directly involved in regular monitoring of UNESCO's extrabudgetary activities, and to that effect needs to be provided with better tools to allow such monitoring. In addition, UNESCO is increasingly called upon to provide regular substantive and financial reporting to the Executive Board and the General Conference, both on extrabudgetary activities proper, and on the interplay between these activities and UNESCO's regular programme. The operational solutions identified below reflect the following guiding principles:

- Regular monitoring of extrabudgetary activities will be institutionalized in UNESCO at several levels with the main focus on the sector ADGs. Overall monitoring will be undertaken, at least twice a year, by the College of ADGs, and at least once a year by the Directorate;
- Adequate monitoring/reporting modalities, including both quantitative and qualitative "Sector Alert Systems" will be developed to provide for early warning and remedial action. Summary reports will be presented to the College of ADGs and the Directorate prior to their reviews;
- Consideration will be given to the possibilities of making UNESCO's internal and external reporting on extrabudgetary activities more "visual", thereby further enhancing the Organization's outreach and visibility;

- An INF document on extrabudgetary activities will be presented, under the overall coordination of ERC/CFS, to each spring session of the Executive Board (since reliable statistical data on extrabudgetary activities during the preceding year will not be available in time for the preparation of a fully-fledged report to that session), with a more in-depth discussion to take place during the fall session if desired by Member States;
- An overall report on extrabudgetary activities, and their interplay with the regular programme, will be presented to each session of the General Conference.

Policy decision and implementation processes

21. **Policy decision:** UNESCO will greatly reinforce its monitoring of extrabudgetary activities, comprising both regular internal monitoring at various levels with the main focus on the programme sector ADGs, as well as regular reporting to the Executive Board and the General Conference

22. Implementation processes

- A “Sector Alert System” will be established for each programme sector to allow a three-monthly review of extrabudgetary activities that have had no, or largely insufficient, financial disbursement during the preceding period, or which are in danger of overspending compared to available cash. Such projects will be identified by BB and DCO, comprising both centralized and decentralized projects, and a report submitted to the ADG (via the relevant AO) prior to the review.
- On the same occasion, i.e. every three months, the programme sectors will conduct an overall review of extrabudgetary activities that may be experiencing substantive difficulties, and that may be in need of revision of the project design. Periodic summary reports to that effect, comprising both centralized and decentralized projects, will be established by the EOs in cooperation with the relevant AO, as well as with ERC/CFS, and submitted to the sector ADG prior to the review.
- Summaries will be prepared of the above reviews by the sector EOs/AOs and submitted to ERC/CFS for advice as to whether the funding sources and/or beneficiaries should be contacted for possible action on the problems.
- Decisions during the reviews will be recorded in SISTER, and systematic follow-up action monitored by the sector EOs/AOs.
- The Committee on Budget and Finance (CBF) will conduct, twice a year, an overall review of all extrabudgetary activities with the main focus on projects experiencing slow or no financial disbursement. Summary reports to that effect will be prepared by BB and DCO; and the views of the relevant programme sectors and field offices will be solicited prior to the reviews.
- The College of ADGs will conduct, twice a year, an overall review of all extrabudgetary activities with the main focus on the qualitative aspects of delivery, and on compliance with UNESCO’s overall strategies for the programming of extrabudgetary activities as an extension of the regular programme, and related resource mobilization. Summary reports to that effect will be prepared by ERC/CFS and BSP.
- The Directorate will devote one annual session to an overall policy review of UNESCO’s extrabudgetary activities, based on reports and recommendations from CBF and the College of ADGs.

- Given that the statistical figures for the previous year's extrabudgetary contributions, allocations and delivery rates are unlikely to be available in time for the normal preparation of reports to the spring session of the Executive Board, agreement should be reached with the Chairperson of the Board that this document be presented as an annual INF document based on reasonably reliable preliminary figures. This will allow an overall review by the Board at this stage of "facts and figures" relating to UNESCO's extrabudgetary activities during the preceding year, and the identification of possible policy issues that may be scheduled for debate during the Board's fall session. Reports to both sessions of the Board will be prepared under the overall coordination of ERC/CFS. Agreement will be reached between BB and DCO on the preparation of statistics that will allow the monitoring, for each funding source, of fresh contributions, allocations and disbursements, as well as of the overall geographical and substantive distribution of UNESCO's extrabudgetary activities.
- An item on UNESCO's policies for extrabudgetary activities will be inscribed in the agenda for each session of the General Conference, allowing a general debate on the basis of a comprehensive report on UNESCO's extrabudgetary activities during the preceding biennium prepared under the overall coordination of ERC/CFS.

NEXT STEPS

23. Following the discussions in the Executive Board of the proposals contained in the present information document, and taking into account the main observations made in this context, the next main steps in pursuance of the External Auditor's recommendations comprise the following:

- comprehensive consultations with UNESCO's field offices on the proposals in the above draft action plan to enhance the role of these offices, within UNESCO's overall strategies and procedures for the management of extrabudgetary activities, in resource mobilization, and in implementation of extrabudgetary projects and programmes (May/July 2006);
- discussion, and finalization, of the Table on Delegation of Authority and Accountability (ToAA) on extrabudgetary activities in UNESCO's Delegation and Accountability Committee (DAC) (May/June 2006);
- focused benchmark studies on the strategies and procedures for management of extrabudgetary funds in the most relevant United Nations agencies (FAO, ILO, UNICEF, UNDP, WHO, etc.) to assess what UNESCO can learn from this) (May/June 2006);
- comprehensive consultations with all major stakeholders on the draft action plan on the management of UNESCO's extrabudgetary funds (May/July 2006);
- in the light of the Director-General's approval of the ToAA on extrabudgetary activities, update and distribution of the Guide to UNESCO's Extrabudgetary Activities, and update of the relevant provisions in UNESCO's Administrative Manual (July/September 2006);
- development of appropriate training material, and conduct of targeted training sessions, for UNESCO staff and interested National Commissions, on all aspects of resource mobilization and management of extrabudgetary funds (September until the end of the biennium);
- presentation, to the 175th session of the Executive Board, of finalized proposals on the overall strategies and procedures for the management of extrabudgetary funds (September 2006).