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y la
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FINANCE COMMITTEE

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Secretariat Response to External Auditor Report on Contracts for Local Services

1. At the 110th Session of the Finance Committee the External Auditor presented his report on the “Review of Contracts for Local Services in FAO” contained in document FC 110/9 and drew attention to his recommendations, which included guidelines for outsourcing, balanced weighting of technical and cost factors in evaluations, strengthening the vendor database and improvements to technical specifications.
2. The Secretariat explained that it had reservations regarding the examples quoted in the report and in this regard felt that extrapolating from such isolated examples to draw wider conclusions would not be appropriate. However, the Secretariat had no difficulty with the general nature of the External Auditor’s recommendations. The Secretariat also emphasized that the External Auditor had not identified any irregularities or breach of established rules and procedures.
3. In view of the different perspectives of the External Auditor and the Secretariat, which was not unusual in value-for-money studies, the Committee requested the Secretariat to present a document in its May 2006 session, explaining its response on the findings and recommendations in the audit report, after further consultations with the External Auditor as necessary.
4. This Note explains in more detail the reservations expressed by the Secretariat at the time of the presentation by the External Auditor of the “Review of Contracts for Local Services in FAO”. Clarifications are now provided which deal with two aspects – i.e. (i) the representiveness of the sample and (ii) the appropriateness of applying conclusions drawn from the examples cited to the much larger group of procurement activities actually implemented by the Organization.

The Scope of the Report:

5. The scope of the Report was less representative than reported. External Audit reported that the audited activities represented US\$ 137.6 million or 34% of procurement expenditures

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over Biennium 2002-2003. The correct figure for local service contracts for the 2002-2003 Biennium is approximately US\$ 47 million (or 10%) out of total procurement volume during the same period of US\$ 377 million undertaken by the HQ procurement service. The report also quoted US\$ 127 million contracted for the period January to August 2004, while the actual figure for the whole of 2004 is actually US\$ 64 million. Therefore, the scope of the Review with respect to overall procurement activities was much more limited than that presented.

Extrapolation of conclusions on selected contracts to wider procurement activities:

6. The Review considered very specific and divergent types of contracts including *inter alia* the move of the library at headquarters, work order contracts for specialized information technology services, construction contract in Ethiopia, transportation contract in Iraq, etc. With respect to these contracts it was implied that had recommendations made with respect to these contracts been applied across similar procurement activities significant savings would have been realized. However, given the very specialized nature of these contracts it is not clear that the general recommendations made are in fact applicable to the cases reviewed. Therefore, while the Secretariat takes no issue with the recommendations set out in the Review which are very general, it is of the opinion that the implication that the Organization lost opportunities for savings in some of the cases reviewed is erroneous and further that any suggestion that hypothetical savings in these particular cases can be extrapolated to a larger group of procurement activities is unsupported.

7. Furthermore, the Secretariat is of the opinion that when considering specific contractual activities, general recommendations such as ensuring that contracts be structured so that the Organization can benefit if the actual work differs from that originally foreseen must be considered also in light of other principles such as expenditure level certainty. In some cases, it is more appropriate for the Organization to enter into fixed price contracts that allow for the absorption of minor changes which may sometimes favour the contractor and other times, the Organization. It is not realistic to assume that contractors will readily accept contractual terms that always place the risk of negative changes on it, while providing that positive changes will always benefit the Organization. Considerations of certainty of expenditure are also important in establishing the currency for projects not to be paid with local funds and explains the requirement that contracts issued in connection with Trust Fund projects are generally denominated in US dollars.

8. In some cases, strict application of the general recommendations may not be in the best interests of the Organization and there is a need for flexibility to allow consideration of the specific circumstances of each procurement activity. For this reason, while the Secretariat accepts the general principles set forth in the recommendations, their application to any particular contractual action must also take account of the specific circumstances of that activity to ensure that the overall interests of the Organization are safeguarded.