



African ***Risk Capacity***

Sovereign Disaster Risk Solutions
A Specialized Agency of the African Union

Financial Audit Summary Report

April - November 2016

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Arid soils in Mauritania, 2012. Photo: Oxfam/Pablo Tosco

EXECUTIVE SUMMARY

The African Risk Capacity (ARC) was designed to improve the capacity of AU Member States to manage natural disaster risk, adapt to climate change, and protect vulnerable populations. To do this, ARC offers tools and services to support risk profiling, risk reduction through contingency planning, early warning and disaster risk financing.

Risk financing, in the form of parametric weather insurance to participating governments, is offered through ARC's African-owned financial affiliate, ARC Insurance Company Limited (ARC Ltd). Africa RiskView is an advanced risk assessment, modeling, and early warning software platform used to estimate and trigger readily available funds, via insurance contracts, to African countries hit by

severe weather events and which have purchased coverage at a market-based cost from ARC Ltd.

In ARC's first year of operation, the 2014 Sahel drought triggered payouts to three of the four countries which had purchased insurance: Mauritania, Niger and Senegal. These countries received a total of approximately USD \$26 million to finance response efforts via the provision of pre-planned assistance to affected households.

Following the triggering of the payouts and as part of ARC's monitoring, evaluation and peer-learning processes, the ARC Agency Secretariat commissioned a (i) process¹ and (ii) financial audit of the payouts in all three countries.

1. Kimetrica is a Monitoring & Evaluation and Disaster Risk Management Consulting firm contracted to complete the ARC process audits for the payouts made by ARC Ltd to Niger, Senegal and Mauritania following the 2014 agricultural season.

The purpose of these audits, in addition to compliance evaluation, was to provide a deeper understanding of the development impacts of insurance linked to early intervention, with the intention of addressing a number of questions such as:

- Did early financing from ARC via the insurance payout shorten the time gap between event and response?
- Does ARC have a greater impact on ensuring food security in the event of a drought than alternative financing mechanisms?
- To what extent does ARC protect against asset depletion at the household level, thereby building resilience?
- How was Africa RiskView used in the Final Implementation Plan preparation?
- Did data organisation and availability contribute to preparedness and/or targeting activities?
- To what extent do Africa RiskView risk quantification and ARC's holistic risk management philosophy change the planning or budgeting practices of participating governments?



Recipient of ARC Ltd payout in Senegal, 2015
Photo: African Risk Capacity

The financial audit was intended to enable the Auditor to express an independent professional opinion on:

- Whether the ARC funds received and the expenditures for the Final Implementation Plan (FIP) implementation period were presented fairly in all material respects by the country in the Final Report financial statements and in accordance with the applicable accounting framework; and
- Whether the financial statements provided by the governments agree or reconcile with other information reported to ARC and that funds were spent as described in the Final Report.

In addition, the audit was intended to provide recommendations to Member States on how financial systems and controls could be improved and financial reporting and fiduciary risk management strengthened. The auditor was tasked with formulating recommendations for ARC on improving future financial audits, and drafting guidelines and enhanced Terms of Reference for future auditors.

This report is specifically focused on the financial audit. It provides a summary of the Financial Audit report which was submitted by Deloitte Senegal regarding the payouts in Senegal, Niger and Mauritania following the 2014 drought in the Sahel. It highlights the outcome of the Deloitte Senegal report which concludes that:

the consistency between the financial report and the accounts were **satisfactory** in all three of the countries which received payouts from ARC Ltd for the 2014 drought.

It also provides insight into the key findings of the Audit, lessons learned, and a series of recommendations which the ARC Agency Secretariat will build on to inform improvements in its engagement with Member States around future payout implementation processes.

BACKGROUND

The 2014 Sahel drought triggered payouts from ARC Ltd to three of the four countries insured in the first drought risk pool. The beneficiary countries were Senegal, Niger and Mauritania. These countries had agreed and paid for insurance policy contracts with ARC Ltd to cover their respective 2014 agricultural seasons and received a total of approximately US \$26 million to support their response efforts to the drought event.

ARC Ltd took the necessary measures and disbursed the payouts to Niger, Mauritania and Senegal for these countries to provide assistance to vulnerable populations. The premiums paid, the corresponding coverage limit, and payouts for Niger, Senegal and Mauritania are shown in the table below.

COUNTRY	PREMIUM	COVERAGE LIMIT	PAYOUT
Niger	\$2,580,000.00	\$30,000,000	\$3,341,062.84
Senegal	\$3,600,000.00	\$30,000,000	\$16,485,683.00
Mauritania	\$1,394,373.81	\$9,000,000	\$6,326,368.27



FINANCIAL AUDIT,

The purpose of the financial audit in each country was to enable the Auditor to express an independent professional opinion on:

- Whether the ARC funds received and the expenditures for the FIP implementation period were presented fairly in all material respect by the country in the Final Report financial statements and in accordance with the applicable accounting framework; and
- Whether the financial statements provided by the governments agree or reconcile with other information reported to ARC and that funds were spent as described in the Final Report.

In addition, the audit was intended to provide recommendations to Member States on how financial systems and controls could be improved and financial reporting and fiduciary risk management strengthened. The auditor was tasked with formulating recommendations for ARC on improving future financial audits, including drafting guidelines and enhanced Terms of Reference for future auditors.

As part of this effort, ARC initiated a competitive tender process to secure the services of an independent firm to conduct the financial audits of the ARC payouts. The tender process was issued and managed through the United Nations World Food Programme (WFP)² procurement system and was concluded in February 2016.

Through this process, Deloitte Senegal was selected and commissioned to carry out the financial audits on behalf of ARC between April and June 2016 in Mauritania, Niger and Senegal.

The country visits for the audits were carried out by the Deloitte Senegal team as follows:

- Mauritania: 4 to 7 April 2016
- Niger: 10 to 14 April 2016
- Senegal: 19 to 25 April 2016

2. WFP and ARC Agency have entered into an Administrative Services Agreement, through which WFP provides technical, administrative, personnel, financial and project management services to ARC Agency.

PROCESS & FINDINGS

While Deloitte Senegal began its work in April, it did not submit the final Financial Audit Reports in June 2016 as pre-agreed due to a number of difficulties encountered during the auditing process. Instead, at the request of the ARC Agency Secretariat, Deloitte Senegal provided a report (the Deloitte Report) in July 2016 which described the challenges encountered in conducting the financial audits.

In particular, Deloitte Senegal identified the inability to conduct the audit in compliance with the International Standards on Auditing (ISA) issued by the International Federation of Accountants (IFAC) and specifically according to the ISRS 4000, the IFAC Standard relating to the execution of agreed-upon procedures. It was also stated that as a result, they would not be able to provide a clear audit opinion based on these standards.

Based on this, Deloitte Senegal proposed to issue a report of factual findings as prescribed by ISRS 4000 based on a number of procedures implemented for the execution of the engagement, this constituting (i) Analysis of the Financial Reports' consistency with the Programme's Books and (ii) a Review of Expenses.

This proposal was submitted to the ARC Agency Governing Board for consideration and was subsequently accepted.

Important to note is that the review process for Deloitte Senegal was undertaken and completed before some countries had fully completed implementation of all their response activities because of delays in response implementation. In such scenarios, the final conclusion of Deloitte was issued pending the provision of requisite documentation by respective Governments. Despite the delays, all such outstanding documents were subsequently provided by all the Governments as requested by the review.

Based on this, the Deloitte Senegal report concluded that:

the consistency between the financial report and the accounts were **satisfactory** in all three of the countries which received payouts from ARC Ltd for the 2014 drought.

LESSONS LEARNED & CHALLENGES

- The financial audit exercise was carried out while the ARC funded activities were still underway, therefore it was difficult to capture the full picture of the financial situation with accuracy at the end of the audit period. Although documentation was subsequently provided by Governments on completion of activities, extension of the audit review period/delay in commencement of audit should be considered.
- Moreover, given the number of actors involved in the implementation, the time devoted by the Deloitte Senegal team to each country was not sufficient to do a thorough analysis of the situation.
- The remoteness of some of the vendors, particularly in Niger, made it difficult to interact with these implementing partners and receive the information requested on time.
- The audit team was not able to have access to the National Treasury accounts of the respective Governments. This made it impossible to secure the Treasury Statement. Access to National Treasury accounts by non-state actors is not standard practice in public financial management and, going forward, such realities must be more carefully considered in the FIP financial audit development process.

- The international standardized auditing framework originally identified in the Terms of Reference to be applied by the auditors in their evaluation of the payouts in the three countries emerged as practically unfeasible. This made it challenging for Deloitte Senegal to carry out the financial audit in accordance with these standards. Going forward there will be a need for greater linkages and guidance on this aspect of the ARC financial audit development process and Public Financial Management (PFM) community.
- It is also important to note that a major contributory factor in the delay around the finalisation of the audits was the availability of the auditors from Deloitte Senegal. Due to closure of the offices and company training schedules, the Deloitte Senegal offices were closed for extended periods and this affected the timeliness around the completion of the reports.
- Although agreed in the audit contract, Deloitte Senegal, to date, has not provided recommendations to ARC on how Member States can improve their financial systems and controls and financial reporting systems in order to strengthen fiduciary risk management. Additionally, no formal recommendation has been formulated or provided to ARC on the improvement of future financial audits, drafting guidelines and enhanced Terms of Reference for future auditors, thereby reducing some of the intended benefits from this process.

RECOMMENDATIONS

Based on the aforementioned and in engagement with Member States, the following are a number of recommendations which the ARC Agency Secretariat will be actively considering as part of an improvement of future financial audits of payouts to Member States:

- Encourage Member States to allocate payouts into special accounts authorised by the Ministry of Finance rather than central Treasury accounts. The 2014 payout experiences demonstrated that disbursing payout funds into national treasury accounts can create hurdles for the quick channelling of funds to implementing structures and partners. This can lead to delays in delivery of response and assistance to beneficiaries. A dedicated account for an ARC Ltd payout would be preferable and will be one of the recommendations made to Member States in the development of their FIPs.
- Recruiting a firm outside of countries where payouts have been made highlighted that this can lead to inefficiency and delays during the audit exercise. Such recruitment can lead to limitations in the extent of the on-ground presence required for such exercises. The Deloitte Senegal team had a limited time of four working days to collect information required and consult with government officials. It is recommended that going forward the recruitment of local, competent firms to conduct the audits would be the most efficient and appropriate approach.
- In order to conduct the audit effectively and provide an opinion, it is necessary to ensure that the audit firm has the ability to have access to countries accounting books or are able to propose methodologies that facilitate access to requisite information to inform audit opinions in line with international and public sector auditing standards. To support this process, countries should be informed and engaged well in advance to gather and discuss possible approaches and the information required to support an efficient auditing process.

ANNEX I Overview of the Contingency Planning Standards & Process

An ARC Contingency Plan comprises two parts (collectively, the Plans), which, together, constitute the Contingency Plans described in the Establishment Agreement³:

1. An Operations Plan includes information regarding: the country's natural disaster risk profile, risk transfer parameters, planned interventions, and draft implementation plans for each possible activity proposed. A country must have an Operations Plan in order to qualify for a Certificate of Good Standing (CGS).
2. A Final Implementation Plan (FIP) details information on how an ARC Ltd payout will be deployed after a specific natural disaster event.

Countries work closely with the ARC Agency Secretariat (the Secretariat), through the ARC In-Country Capacity Building Programme (the Capacity Building Programme), to prepare to take out insurance. As part of the Capacity Building Programme, countries:

1. review, validate, and customize Africa RiskView, as necessary⁴;
2. determine risk transfer parameters;
3. develop an Operations Plan (with the support of the Secretariat, if so requested); and
4. identify further capacity building and/or support needs to address identified gaps in country disaster risk management⁵.

Although many of the ARC requirements and standards are consistent across different categories of natural disasters, there are important differences in the preparation for each. Therefore, each natural disaster has its own capacity building workstream and a country must enter into separate insurance contracts for each peril. A country may engage in these workstreams simultaneously, or consecutively, depending on the resources of ARC and the needs of the country.

3. See the Establishment Agreement, Articles 13 (h and i) and 15 (k-l).

4. The extent to which a country must customize Africa RiskView depends on the type of natural disaster for which it is seeking insurance coverage. In all cases it must validate Africa RiskView modeled results for past natural disasters.

5. ARC seeks to help countries identify means in which their disaster risk management structures may be supported through existing capacity building initiatives. ARC intends to act as an interlocutor with agencies offering assistance in key disaster risk management areas and to ensure that countries are supported to receive appropriate capacity investments to support their Disaster Risk Management activities.

Operations Plans

When an Operations Plan is finalized through in-country processes, the country submits it to the Secretariat, which in turn submits it to the Technical Review Committee (TRC) comprised of seven independent experts. The TRC reviews and evaluates the Operations Plan, and provides a report of its assessment (the TRC Report) to the Peer Review Mechanism (PRM) of the Board.

The PRM, which includes three members of the Board, conducts its own independent evaluation of the Operations Plan, taking into consideration the TRC Report. The PRM then issues a report to the full Board (the PRM Report) with its recommendations regarding whether the Operations Plan has met the criteria set by the Board.

The Board takes the final decision regarding whether an Operations Plan has met the CP Standards.

Final Implementation Plans

Prior to an ARC Ltd payout, a country is required to submit a FIP through a process similar to the Operations Plan submission process, and the Secretariat will provide support to the country for its FIP development, if so requested. The FIP, which includes detailed information on how an ARC Ltd payout will be deployed during a specific natural disaster, should only include activities that have already been approved as part of the country's Operations Plan, unless there is a clear justification provided, for example, in the case of a rapid-onset disaster or in the identification of specific unforeseen needs outside of those considered in the Operations Plan. If a country would like to include additional activities that were not already approved as part of the Operations Plan, it must also subsequently amend its Operations Plan.

Once a country has finalized its FIP, it shall submit the FIP to the Secretariat for onward transmission to the TRC and PRM.

Drought Response FIPs

If a country is submitting a FIP for drought response, it shall make the submission when it is determined that an insurance payout is likely .

When a country has finalized its FIP, the TRC reviews the FIP and provides its comments to the country and the PRM. The PRM then reviews the FIP and the TRC Report, and provides its comments to the full Board. If the TRC and PRM determine that the FIP should be strengthened, it may be sent back to the country for revisions, after which time the TRC will re-review the FIP.

Once the TRC and PRM are satisfied that the FIP meets the standards adopted by the Board, the FIP is presented to the Board along with the TRC Report and the PRM Report. The Board takes the final decision regarding FIP approval. Once the FIP is approved, ARC Ltd will release the payout to the country.

6. Likely in this case is defined as: 1) when the certainty of an insurance payout is greater than 70% within 60-70 days of the potential payout date; or 2) if, at the end of the sowing window defined in the insurance contract, it is determined that a country will be entitled to an insurance payout, regardless of the rainfall conditions for the remainder of the insured season. The Director General may also declare that a payout is likely based on the monitoring of the Africa RiskView Software.