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Enabling poor rural people
to overcome poverty

Workplan for IFAD's Office of Audit and Oversight for 2011

Note to Executive Board representatives

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Workplan for IFAD's Office of Audit and Oversight for 2011

I. Introduction

1. The Office of Audit and Oversight (AUO) provides independent and objective assurance and advisory services designed to add value and improve the operations of IFAD. It helps IFAD accomplish its objectives by using a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes. AUO also reviews and investigates possible or alleged irregular practices, including staff misconduct, fraud and corruption in IFAD activities.
2. AUO is committed to strengthening organizational effectiveness by providing assurances to Management as to the efficient management of the Fund's budget and human resources and its internal processes, as well as fostering a culture of accountability, quality, continuous improvement and integrity in IFAD activities and operations. The pursuit of these institutional goals is the guiding priority for AUO in shaping its annual plan.
3. This report presents the AUO workplan for 2011 together with information about the basis upon which it was developed. Input for its formulation was sought from Senior Management and it has been approved by the President. The activities outlined in the workplan are intended to assist Management and the Audit Committee of the Executive Board in determining whether the internal controls related to financial administration and internal oversight are adequate. The Audit Committee may, in accordance with its terms of reference, make proposals for the workplan for the consideration of the President, and, once finalized, the workplan is submitted for confirmation to the Executive Board.

II. Internal audit assurance and advisory activities

Nature of internal audit activities

4. In conducting internal audit assurance activities, AUO determines the scope of its work independently, generally assessing whether IFAD's risk management, control and governance processes are adequate to ensure that:
 - Financial, managerial and operational information is accurate, reliable and timely;
 - Activities comply with policies, standards, procedures, agreements and applicable laws and regulations;
 - Assets and resources are acquired, utilized and protected appropriately; and
 - Programmes, plans and objectives are achieved.
5. Assurance reports include an overall audit opinion communicating the significance of audit results. Audit opinions classify audit results as **satisfactory**, **needs improvement** or **unsatisfactory**, indicative of the following:
 - **Satisfactory:** Risk management, control and governance processes are adequate and effective to provide reasonable assurance regarding the achievement of control and/or business objectives under review. Opportunities for improvement may nevertheless exist.
 - **Needs improvement:** Deficiencies exist in risk management, control or governance processes, such that reasonable assurance regarding the achievement of control and/or business objectives under review may be at risk.

- **Unsatisfactory:** Significant and/or pervasive deficiencies exist in risk management, control or governance processes such that reasonable assurance regarding the achievement of control and/or business objectives under review cannot be provided.
6. The nature and scope of advisory services are agreed with Management and may involve providing advice or analyses to promote improvements without assuming Management's responsibility for implementing processes, in order to avoid conflicts of interest. Advisory reports do not include an overall opinion but may nevertheless make recommendations to be followed up by AUO.

Risk assessment as the basis for the AUO workplan

7. In accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing* and following the practice of previous years, AUO's 2011 plan was prepared on the basis of a risk assessment exercise. This involved consideration of various sources of input, including the following:
- Financial implications (materiality) of operations;
 - Key objectives of the Eighth Replenishment, corporate management results and the Medium-term Plan;
 - Emerging issues in minutes of Senior Management (IFAD Management Team, Executive Management Committee [EMC] and Operations Management Committee) and Audit Committee meetings;
 - Corporate risk registers and the corporate risk profile;
 - Distribution of open and overdue audit recommendations;
 - External audit workplans and reports;
 - History of internal audit activities (or absence thereof) and accumulated concerns in each area; and
 - Discussions with EMC members.
8. The proposed workplan is being presented to the Audit Committee much earlier than in previous years so that the size and complexity of the workplan can be considered together with the 2011 budget proposal for the Office of Audit and Oversight. This will allow the Committee to better assess the necessary resources or the feasibility of the proposed workplan. Given the timing of this paper, the input factors considered for the risk assessment are limited to the status as of early September 2010 and consequently two assignments have been left to be determined in the light of emerging risks during 2011. While the staffing of AUO is currently undergoing major change, the 2011 workplan assumes that the team will be operating at full strength.

Internal audit activities planned

9. Given the very ambitious workplan approved for 2010 and the length of the audit cycle, five audit engagements initiated in 2010 will still be in progress, scheduled for completion in early 2011. For 2011 there will also be seven assurance engagements (including two recurrent and one carried forward from the 2010 workplan that has not yet been started), and five advisory engagements are proposed. Having developed and piloted a methodology for country programme audits in 2010, at least two **audits of country programmes** are now expected to be a recurrent element in the yearly workplans. In addition, after the successful launch of the internal audit capacity development initiative in 2010, this will also be an ongoing activity, requiring approximately two **capacity assessments** and ongoing support for the participants who started in 2010 and those yet to arrive.
10. Given that the AUO workforce in 2011 will include a new audit officer (replacing a colleague who retired at the end of April 2010), a new investigation officer

(replacing a colleague who departed in July 2010) and several capacity development participants, the workplan has been formulated to include audits with a mix of complexity and geographical coverage, covering both in-country offices and headquarters issues.

11. AUO will maintain its ongoing membership in either an **observer or an advisory support capacity** in various working groups, committees and ad-hoc committees, including the Enterprise Risk Management Committee, the Country Presence Working Group, the Working Group on Knowledge Management and Innovation, and the Information Technology Governance Committee. The AUO Director or representative also attends the meetings of the IFAD Management Team, the Operations Management Committee and the Investment and Finance Advisory Committee to maintain awareness and understanding of key activities of the organization and to support the organization in addressing emerging risks and challenges in a timely manner.
12. Until the new Ethics Office is fully established and staffed, AUO will be managing ad interim the recently established **certification of compliance with the Code of Conduct**. In addition, in view of the internal auditing standards that calls for an external quality assessment of the internal audit function at least once every five years, an internal quality assessment will be undertaken during 2011 in preparation for the next external assessment in 2012.

III. Investigation activities

13. Within AUO, the Investigation Section is mandated¹ to **investigate** as appropriate all matters related to irregular practices in IFAD activities and operations. Irregular practices include staff misconduct, and fraud and corruption in relation to entities, contractors and non-staff individuals applying for or participating in IFAD-financed activities or headquarters-related contracts.
14. The main activities of the Investigation Section will include **promoting and advocating for IFAD's anticorruption policy**, conducting and administering investigations, and serving as secretariat to the Sanctions Committee. Engagement and collaboration with PMD, including training, will continue to be a priority. Visibility in field operations will continue to be emphasized by pursuing effective engagement with project staff. In addition, the Investigation Section will support the establishment of the newly defined Ethics Office to ensure that the roles and processes of the two functions are complementary and yet fully distinct.

IV. Workplan for 2011

Planning risks

15. The nature of audit and investigation work makes it difficult to predict the actual level of effort required to conclude individual engagements. All assignments may be subject to rescheduling or reconsideration of priority and scope at the time of initiation, based on a preliminary review of the risk environment and mitigating controls at that time. The modest size of AUO limits its ability to maintain in-house skills appropriate to conduct all the work; therefore, consulting and short-term specialist expertise is used to supplement skills on a temporary basis as appropriate.
16. Steps were initiated in 2010 to improve and expand the human resource base and overcome resource limitations. Recruitment processes for an audit officer and an investigation officer were completed in 2010. Although AUO requested an associate professional officer for the Audit Section and placed more emphasis on the field aspect of audit work to attract more interest, no one has yet been proposed. An initiative to support the development of the internal audit capacity in the government ministries of IFAD's borrowing countries was successfully launched in

¹ President's Bulletin 2007/02 of 21 February 2007, section 2.4.1.

2010 and, as a result, three participants have come to work with AUO for a six-month period each. Although this requires an investment of time by AUO staff, these participants supplement the AUO professional resources and are a source of reciprocal knowledge sharing for the AUO staff. Plans are already in place to identify additional participants who would begin as the first participants complete their development period.

17. As is the usual practice, several activities from the 2010 workplan have been started and will be completed in early 2011, and several were moved forward to the 2011 plan in response to changing priorities. The AUO workplan is a rolling plan in that it is an ongoing pipeline of activities that responds to the evolving risk environment. The proposed activities are set out in table 1 below.

Table 1
AUO workplan for 2011

	<i>Percentage</i>	<i>Number of staff days</i>
Internal audit activities	52	936
<i>Assurance engagements</i>		
1. Accounting items requiring Management estimates or assumptions (started in 2010)		
2. Entity-level review of control environment (started in 2010)		
3. IT Network Security (started in 2010)		
4. Follow-up country presence memoranda of understanding arrangements (started in 2010)		
5. Follow-up consultant management (started in 2010)		
6. Certification of expenditure to be reimbursed by the Government of Italy (recurrent)		
7. OP Expenses for 2010 (recurrent)		
8. Follow-up grant management, supervision, record-keeping (carried forward from 2010 plan)		
9. Country programme audit #1		
10. Country programme audit #2		
11. Institutional contracts usage and process		
12. Investment in training of human resources		
13. <i>to be determined</i>		
14. <i>to be determined</i>		
<i>Advisory engagements</i>		
15. Reporting on divisional key performance indicators (KPIs)		
16. Develop field staff anticorruption and internal audit training module (carried forward from 2010)		
17. Develop testing structure for management assertion on internal controls over financial reporting (continuation based on completed readiness assessment)		
18. Capacity development assessment #1		
19. Capacity development assessment #2		
Investigation activities	25	450
20. Promoting and advocating for IFAD's anticorruption policy		
21. Investigative work		
Office management and capacity-building	23	414
22. Support establishment of new Ethics Office		
23. Secretariat support to investigations and sanctions processes		
24. Office capacity-building (internal quality assessment, audit manual updates, development and maintenance of audit support tools)		
25. Staff training and development of new staff and capacity development participants		
26. Representation in internal and external meetings		
27. Office management and administration		
Total AUO staff days	100	1 800

Audit activities from 2010 to be completed in 2011

18. A review of **accounting items requiring Management estimates and assumptions** was planned for 2010 due to their materiality and because it is useful for internal audit to understand the management of these items in looking towards supporting the Management assertions on internal controls over financial reporting. Work on this audit was started in the fourth quarter of 2010 and is also being supported by one of the capacity development candidates as a very relevant learning opportunity.
19. It was decided in 2010 to perform a review of the **entity-level control environment**, which was initiated in the fourth quarter of 2010 with the support of a highly experienced external audit professional. The final report is expected to be completed in early 2011 depending on feedback and discussion with Management. Although elements of the control environment are regularly reviewed indirectly in the context of most internal audits, the control environment as a whole has never been assessed in a structured and comprehensive manner by AUO and is therefore an important as well as a complex audit.
20. A key audit of the **IT network security** was started in the second half of 2010 with the support of external technical experts, who were selected in a competitive procurement process for this complex audit. The final report is to be completed with feedback from Management in early 2011.
21. A series of five focused **follow-up audits** were planned in 2010 for areas where high priority recommendations have been outstanding for an extended period of time. The follow-up audits reassess the outstanding issues to determine whether risks have been partially or fully mitigated by process changes or other compensating measures, or to validate and define more clearly the priority for actions to address risks. One of these follow-up audits was finalized in 2010,² one on communications strategy and service was cancelled based on the AUO risk assessment, and three more were started in the last part of 2010 in the following areas:
 - **Consultants management;**
 - **Grant management supervision and record-keeping; and**
 - **Country presence memoranda of understanding arrangements**

Internal audit assurance engagements proposed for 2011

22. Having developed and piloted an audit programme for country programmes in 2010, AUO expects to include **audits of at least two country programmes** as recurrent elements in the annual workplan. This will allow AUO to gain an understanding of IFAD's field activities, which will contribute directly to improving the quality of other audit work. These audits will also serve to assure Management that monitoring processes are performed outside of IFAD headquarters. Project procurement will receive appropriate emphasis.
23. An audit of the **use of and the process for institutional contracts** has been proposed. This area had not been audited before because the process for this type of contract is decentralized and lies outside both the consultant recruitment and the headquarters procurement processes. There is also an indication that the use of such contracts is increasing.
24. **Training expenditures and institutional policy on training** is an area that was identified for review due to the size of its budget (over US\$1 million in 2010) and the important role that investment in training has on IFAD's ability to implement its human resource reform activities and to deliver on the objectives it has set.

² i.e. assessment of borrower/recipient's procurement systems.

25. As in previous years, AUO will perform the recurrent audit activities of reviewing the **certification of expenditures to be reimbursed by the Italian Government** and the audit of the **expenditures of the Office of the President**. Quarterly follow-up on feedback from divisions concerning actions taken to close outstanding internal audit recommendations will also continue to be a key activity of AUO to aid both divisions to understand the related risks and find appropriate solutions.

Internal audit advisory engagements proposed for 2011

26. **Divisional key performance indicators reporting** has been in place for three years now and the decentralized figures and calculations reported by the divisions are used by Management for key decision-making. In some cases, this information flows into corporate-level reporting which is also provided to IFAD's governing bodies. An audit of this area will provide advice to Management that these figures are meaningful and reliable for both reporting and decision-making purposes.
27. AUO plans to develop an **anticorruption and internal audit training module** for delivery to staff, project implementation teams and others at both headquarters and in the field. This module will build an awareness of good governance, risk assessment and mitigation through strong internal controls, and help overcome reluctance, uncertainty and other barriers to coming forward with information and allegations about corruption in IFAD operations. It will also help to mainstream IFAD's anticorruption policy and support capacity development for project supervision.
28. As documenting of the processes and a readiness assessment were completed by the Financial Services Division in 2010, AUO will develop a process for testing **internal controls over financial reporting** in anticipation of a Management assertion on these controls. The process will also build on a readiness assessment performed in late 2010.
29. In 2010, AUO successfully developed and started up the internal audit capacity development initiative, for which three participants are currently working with AUO at the Rome headquarters. Strong interest has been expressed by other IFAD regional divisions and other countries have been identified as potential candidates for participation. To keep this initiative on-going, approximately two **internal audit capacity assessment missions** will be fielded. Time of both auditors and administrative staff needs to be allocated to support the participants already starting in 2010 and those yet to arrive.

V. Budget and resources for 2011

30. At the time of writing this report, the AUO budget proposal for 2011 is still under discussion. Normally staff costs account for 90 per cent of AUO's budget. As is always the case, the number and complexity of investigations is unpredictable and a request for additional resources during the year may be necessary.
31. Expenditures related to internal auditing are expected to account for approximately 70 per cent of the resources and investigations 30 per cent of the total.