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## Revisions to the Financial Regulations of IFAD

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For: **Approval**

## **Recommendation for approval**

The Executive Board is invited to consider the draft resolution on the Revisions to the Financial Regulations of IFAD contained in the annex and to approve its submission to the Governing Council at its thirty-fifth session in February 2012 for adoption.

## **Revisions to the Financial Regulations of IFAD**

1. The present paper has been prepared by the Office of the General Counsel in consultation with the Chief Financial Officer; the Director, Controller's and Financial Services Division; and the Treasurer. It concerns the revisions to the Financial Regulations of IFAD to be submitted for the consideration of the Executive Board (through the Audit Committee) and subsequently to the Governing Council in February 2012.

### **I. Revision to permit proper operation of the carry-forward provision with respect to the several categories of the administrative budget**

#### **I.1. The carry-forward rule should reflect the evolution of budgeting in IFAD**

2. The primary reason for this revision emanates from the 3 per cent carry-forward introduced by Governing Council resolution 133/XXVII (2004). Before the amendment, the rule stated that:
 

"The appropriations voted by the Governing Council for the ensuing financial year shall constitute an authorization to the President to incur obligations and make payments for the purpose for which the appropriations were voted. Unobligated appropriations at the close of the financial year shall be cancelled."
3. The term "unobligated appropriations" means the total unutilized amount at the close of the specified financial year. Since the above-mentioned amendment, regulation VI.2 reads:
 

"The appropriations voted by the Governing Council for the ensuing financial year shall constitute an authorization to the President to incur obligations and make payments for the purpose for which the appropriations were voted. Unobligated appropriations at the close of the financial year may be carried forward into the following financial year up to an amount not exceeding 3 per cent of the said financial year."
4. This triggers the issue of what amount constitutes the basis on which to calculate the 3 per cent carry forward. The question is whether the 3 per cent is determined on the basis of the total unutilized budget at the close of the specified financial year, i.e. the sum of the unobligated appropriations of the administrative budget, the capital budget, and the budget of the Independent Office of Evaluation of IFAD (IOE), or whether the capital budget and/or budget of IOE should be excluded.

#### **I.2. Clarify how the carry-forward rule should operate with respect to the IOE budget and to the capital budget**

5. The clarification sought purports to deal with two issues that have evolved over time: (i) distinguishing between the regular budget and the IOE budget for the purposes of the operation of the carry-forward rule; and (ii) clarification that the capital budget is not subject to regulation VI.2.
6. This clarification is needed because, according to the wording of section 10 of article 6 of the Agreement Establishing the International Fund for Agricultural Development (the Agreement), the Governing Council approves one budget labelled the "administrative budget". In other words, the Agreement envisages only one budget.

This is not changed by the fact that in recent years the presentation of this budget has been divided into an administrative budget, the capital budget, and the IOE budget. In other words, neither the Agreement nor the Financial Regulations envisages three budgets. Since the Governing Council decided that the financial resources for the evaluation function should be distinguishable and that there should be a capital budget, the Governing Council should be asked to amend the Financial Regulations in order to reflect the wish to create a category for IOE and a capital budget within the administrative budget.

7. Since regulation VI deals with the Fund's administrative budget, strictly speaking the 3 per cent applies to the total of the administrative budget, irrespective of the categories within the administrative budget. Indeed, Financial Regulation I makes it clear that "(T)hese regulations ... shall be interpreted in accordance with the Agreement." However, notwithstanding the foregoing, it seems that in practice, when the 3 per cent is calculated, no account is taken of the unutilized amounts under the capital and IOE budgets. Experience has revealed that there are instances where IOE needs to carry forward unobligated appropriations in order to take on unanticipated activities.
8. There is no record showing that when the 3 per cent carry forward was introduced in 2004 by the Governing Council, consideration was given to the consequences for the capital budget, introduced in 2001 (Governing Council Resolution 116/XXIII, 2000), and/or the budget of IOE.
9. The technical implications of the foregoing oversight can be easily corrected and brought back into line with the practice hitherto. To eliminate any doubt, it is recommended that regulation II and regulation VI be amended to include the following points and will read as follows:

#### **Regulation II**

- (h) "Administrative budget" means the annual administrative budget of the Fund referred to in article 6, section 10 of the Agreement Establishing IFAD, which shall consist of a regular budget, a capital budget and an Independent Office of Evaluation of IFAD budget;
- (i) "Regular budget" means the category of the administrative budget voted by the Governing Council for the administration of the Fund, excluding the Independent Office of Evaluation of IFAD and the capital budget;
- (j) "Capital budget" means the category of the administrative budget voted by the Governing Council for commitments and payments to finance capital items, the cost of which are normally written off over a number of financial years making up the estimated useful life of the asset;
- (k) "Independent Office of Evaluation of IFAD budget" means the category of the administrative budget voted by the Governing Council for the administration of the Independent Office of Evaluation of IFAD.

#### **Regulation VI**

1. The President shall submit an annual administrative budget estimate to the Executive Board for transmission to the Governing Council for approval by a two-thirds majority of the total number of votes.
2. The appropriations for the regular budget and for the Independent Office of Evaluation of IFAD budget voted by the Governing Council for the ensuing financial year shall constitute an authorization to the President to incur obligations and make payments for the purpose for which the appropriations were voted. All unobligated appropriations under the regular budget and the Independent Office of Evaluation of IFAD budget, respectively, at the close of the financial year may be carried forward into the following financial year up to an amount not exceeding 3 per cent.

3. To meet the Fund's requirements the President may, with the approval of the Executive Board, reallocate funds between categories of the administrative budget.
4. Without prejudice to paragraph 3 above, the appropriations for the capital budget voted by the Governing Council for the ensuing financial year shall constitute an authorization to the President to incur obligations and make payments for the purpose for which the appropriations were voted.
  - (i) The appropriations for the capital budget voted by the Governing Council shall be used exclusively for commitments and payments to finance long-term outlays.
  - (ii) All unobligated appropriations under the capital budget voted by the Governing Council at the close of the third financial year shall be cancelled unless the Governing Council decides otherwise.

## **II. Strengthening the role of the Executive Board with respect to the investment policy**

### **II.1. Need to strengthen the Executive Board's role**

10. In light of the evolution of the organization and the increased size and complexity of its investment practices, the President deems it advisable to revisit the division of labour currently in the Financial Regulations whereby the President adopts the investment policy under Financial Regulation XIII. It is deemed more appropriate that the Executive Board be given a decisive role in this matter. For this purpose, it is proposed that Financial Regulation VIII.2 be amended to read as follows:
 

"In investing the resources of the Fund, the President shall be guided by the paramount considerations of security and liquidity. Within these constraints, **and subject to the policy statement laid down by the Executive Board**, the President shall seek the highest possible return in a non-speculative manner."
11. In anticipation of these changes, Management informed the Executive Board during an informal seminar prior to the 102<sup>nd</sup> session of the Board that an investment policy inclusive of a full investment policy statement would be submitted for approval in September 2011. The Executive Board considered IFAD's Investment Policy Statement (EB 2011/103/R.33) and its accompanying background note (EB 2011/103/R.32) and agreed that a final investment policy statement would be submitted to the Audit Committee for its review prior to submission to the Executive Board for approval at its December 2011 session.

## **III. Codification**

### **III.1. Regulation XII**

12. Paragraph 1 of this regulation has been amended to reflect the decision of the Governing Council in resolution 77/2 whereby the Council delegated its authority to the Executive Board in matters relating to the appointment of the external auditor. For this purpose, it is proposed that Financial Regulation XII.1 be amended to read as follows:
 

"The accounts of the Fund shall be audited at least once a year by a qualified and independent external auditor **appointed by the Executive Board**."

### **III.2. New regulation XIII**

13. A new regulation "Financial Regulation XIII – General Reserve" is created to reflect the establishment of the General Reserve. This is based on past decisions of the Governing Council (resolutions 16/IV and 111/XXII). For this purpose, it is proposed that a Financial Regulation XIII be created to read as follows:

**“Regulation XIII – General Reserve**

A General Reserve shall be established to cover the Fund’s potential over-commitment risk as a result of exchange rate fluctuations and possible delinquencies in the receipt of loan service payments or in the recovery of amounts due to the Fund from the investment of its liquid assets.

The following provisions shall be implemented with respect to the General Reserve:

- (a) Annual transfers from the accumulated surplus to the General Reserve shall be determined by the Executive Board after taking into account the Fund’s financial position;
- (b) The adequacy of the General Reserve shall be periodically reviewed by the Executive Board;
- (c) Subject to the above, the ceiling of the General Reserve may be amended from time to time by the Executive Board;
- (d) Withdrawals from the General Reserve shall be subject to the prior approval of the Executive Board.”

14. Former regulation XIII will now become regulation XIV.

## Resolution .../XXXV

### Draft Resolution on the Revisions to the Financial Regulations of IFAD

#### The Governing Council of IFAD,

**Acting** under article 6, section 2(f) of the Agreement Establishing IFAD;

**Recalling** resolution 133/XXVII adopted by the Governing Council at its twenty-seventh session in 2004 amending regulation VI, paragraph 2 of the Financial Regulations of IFAD, to allow unobligated appropriations at the close of the financial year to be carried forward into the following financial year up to an amount not exceeding 3 per cent of the said financial year;

**Recalling** that the Governing Council at its twenty-third session in 2001 approved, in its resolution 116/XXIII the introduction of the capital budget into the administrative budget;

**Further recalling** that the Executive Board at its seventy-eighth session in April 2003 approved the IFAD Evaluation Policy, which established the principle of a separate annual budget as part of the administrative budget;

**Aware** that a final Investment Policy Statement would be submitted to the Audit Committee for its review prior to submission to the Executive Board for approval at its December session in 2011;

**Having considered** resolution 77/2 whereby the Governing Council delegated its authority to the Executive Board in matters relating to the appointment of the external auditor;

**Having considered** resolution 16/IV and resolution 111/XXII whereby a General Reserve was established;

Decides that:

- I. Regulation II of the Financial Regulations of IFAD shall be amended to read as follows:

#### Regulation II

- (h) "Administrative budget" means the annual administrative budget of the Fund referred to in article 6, section 10 of the Agreement Establishing IFAD, which shall consist of a regular budget, a capital budget and an Independent Office of Evaluation of IFAD budget;
- (i) "Regular budget" means the category of the administrative budget voted by the Governing Council for the administration of the Fund, excluding the Independent Office of Evaluation of IFAD and the capital budget;
- (j) "Capital budget" means the category of the administrative budget voted by the Governing Council for commitments and payments to finance capital items, the cost of which are normally written off over a number of financial years making up the estimated useful life of the asset;
- (k) "Independent Office of Evaluation of IFAD budget" means the category of the administrative budget voted by the Governing Council for the administration of the Independent Office of Evaluation of IFAD.

- II. Regulation VI of the Financial Regulations of IFAD shall be amended to read as follows:

**Regulation VI**

1. The President shall submit an annual administrative budget estimate to the Executive Board for transmission to the Governing Council for approval by a two-thirds majority of the total number of votes.
2. The appropriations for the regular budget and for the Independent Office of Evaluation of IFAD budget voted by the Governing Council for the ensuing financial year shall constitute an authorization to the President to incur obligations and make payments for the purpose for which the appropriations were voted. All unobligated appropriations under the regular budget and the Independent Office of Evaluation of IFAD budget, respectively, at the close of the financial year may be carried forward into the following financial year up to an amount not exceeding 3 per cent.
3. To meet the Fund's requirements the President may, with the approval of the Executive Board, reallocate funds between categories of the administrative budget.
4. Without prejudice to paragraph 3 above, the appropriations for the capital budget voted by the Governing Council for the ensuing financial year shall constitute an authorization to the President to incur obligations and make payments for the purpose for which the appropriations were voted.
  - (i) The appropriations for the capital budget voted by the Governing Council shall be used exclusively for commitments and payments to finance long-term outlays.
  - (ii) All unobligated appropriations under the capital budget voted by the Governing Council at the close of the third financial year shall be cancelled unless the Governing Council decides otherwise.

- III. Regulation VIII.2 of the Financial Regulations of IFAD shall be amended to read as follows:

**Regulation VIII.2**

In investing the resources of the Fund, the President shall be guided by the paramount considerations of security and liquidity. Within these constraints, and subject to the policy statement laid down by the Executive Board, the President shall seek the highest possible return in a non-speculative manner.

- IV. Regulation XII.1 of the Financial Regulations of IFAD shall be amended to read as follows:

**Regulation XII.1**

The accounts of the Fund shall be audited at least once a year by a qualified and independent external auditor appointed by the Executive Board.

- V. A new regulation "Financial Regulation XIII – General Reserve" is created to reflect the establishment of the General Reserve:

**Regulation XIII – General Reserve**

A General Reserve shall be established to cover the Fund's potential over-commitment risk as a result of exchange rate fluctuations and possible delinquencies in receipt of loan service payments or in the recovery of amounts due to the Fund from the investment of its liquid assets.

The following dispositions shall be implemented with respect to the General Reserve:

- (a) Annual transfers from the accumulated surplus to the General Reserve shall be determined by the Executive Board after taking into account the Fund's financial position;
  - (b) The adequacy of the General Reserve shall be periodically reviewed by the Executive Board;
  - (c) Subject to the above, the ceiling of the General Reserve may be amended from time to time by the Executive Board;
  - (d) Withdrawals from the General Reserve shall be subject to the prior approval of the Executive Board.
- VI. Former regulation XIII will now become regulation XIV.
- VII. This resolution and the revisions to the Financial Regulations of IFAD shall enter into force upon the adoption of this resolution and shall have effect from financial year 2012.