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Report of the Chairperson on the 124th meeting of the Audit Committee

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Executive Board — 106th Session
Rome, September 2012

For: **Review**

Report of the Chairperson on the 124th Meeting of the Audit Committee

1. The Audit Committee wishes to bring to the attention of the Executive Board the matters examined at the 124th meeting of the Committee held on 17th September 2012. The representative for the Netherlands assumed the Chair and informed that the Committee Chairperson was unable to attend due to personal matters and sent her apologies. The new representative of Sweden was introduced to the Committee.

Adoption of the agenda

2. The agenda was adopted with the postponement of item 7 of the agenda, Consultants Management Procedures. This item will be considered at the 125th session of the Audit Committee, scheduled to take place in November.

Minutes of the 123rd meeting of the Audit Committee

3. The Committee approved the Minutes of its 123rd meeting without any comments.

High-level preview of IFAD's 2013 results-based programme of work and administrative and capital budgets, and preview of the Independent Office of Evaluation of IFAD's results-based work programme and budget for 2013 and indicative plan for 2014-2015

4. The chairperson introduced the item and invited Management to present the document.
5. Management reminded the Committee that the document being presented was a high-level document, setting out broad parameters for 2013. A final budget, encompassing results of the current Strategic Workforce planning exercise and inputs from all IFAD's Departments, would be presented to the Committee in November 2012, before being submitted to the Executive Board for approval in December 2012.
6. The Committee was further informed that in relation to the programme of loans and grants financed from IFAD's regular resources, Management is proposing an amount of US\$1.06 billion, a slight increase on the expected US\$1.01 billion currently forecast for 2012. With regard to the administrative budget, management proposed an amount of US\$144 million in 2012, which represented an overall nominal increase of 2.5% mainly due to the inflation factor. Due to the difficult fiscal climate and management's focus on efficiency, a zero nominal increase in the budget for 2013 is being proposed.
7. A slight decrease in cluster 1 from 61.4% in 2012 to 59.8% of the total budget is being planned in 2013. In part, this reduction is due to the re-centralization of certain costs such as recruitment.
8. Management is focusing on achieving a higher level of efficiency during the 9th Replenishment period which may entail changes in budget allocations across clusters.
9. The Committee was informed that an analysis of 2011 actual and 2012 forecast costs show that key areas such as IT urgently require more funding to deliver the services that are being demanded by operations.
10. Other areas brought to the Committee's attention were Management's decision to present gross and net budgeting. Gross budgeting will include the

administrative budget and the cost of activities supporting Supplementary Funds (SF) and special projects, while the net administrative budget will exclude the cost of SF activities. Approval will only be sought for the net administrative budget. An estimate of US\$4.0 million is envisaged for the capital budget.

11. The Independent Office of Evaluation presented the report on its results-based work programme and budget for 2013 and indicative plan for 2014-2015 and highlighted that it had been prepared in close discussion with IFAD Management. Key issues raised were as follows:
 - The Evaluations Committee had reviewed the high-level preview document of IOE at its July session and suggestions made would be taken into account in preparing the next iteration of the document.
 - The Committee was informed that IOE followed the results-based work programme and budget approach and linked its resource needs to the work being proposed and the divisional management results.
 - The list of final proposed evaluations would be finalized soon after the Board meeting and further consultation with IFAD Management, which could possibly impact the final version of the 2013 budget. This final work programme and budget would be submitted to the Evaluation Committee in October, the Audit Committee in November and to the December Executive Board for approval.
 - IOE's staff composition was being reviewed in light of the IFAD wide job audit and the strategic workforce plan. In this context, IOE expected to reduce its staff by one position.
 - IOE proposed budget for 2013 is around US\$6million.
12. The Chair thanked Management and IOE for the presentation and invited comments from members.
13. On the IFAD administrative and capital budgets, comments from members included requests for clarification on how IFAD envisaged pursuing high level policy dialogue; clarification on the programme of loans and grants numbers presented in the high-level preview document for the 2012 budget discussed at the 120th meeting of the Audit Committee as compared to those contained in the current document; confirmation of the regional allocation of the programme of work foreseen for Asia and Latin America, specifically in view of the 40-50 per cent assigned to Sub Saharan Africa; clarification on why the programme of work covers six thematic areas, while the IFAD Strategic Framework 2011-2015 contained eight, with non-farm employment and technical and vocational training seemingly missing.
14. Other comments included a call for Management to reduce administrative costs; reason for the reduction in the loan reflows and supplementary funds fees in the medium term budgetary projections; and, clarification on the distribution of the lending and DSF grants by thematic area relating to reduction of hunger and poverty.
15. A concern was raised on the reduction in projected funding for the area of effective and efficient functioning of IFAD's governing bodies, with two members asking if this would affect the provision of translation and interpretation services.
16. Members raised the possibility of considering the IFAD and IOE budgets in two separate documents.
17. Whilst welcoming the zero growth projection, members called for more information on internal distribution, including an overview of its evolution.

Other comments included a request for more information on actuals for 2011 and, as far as possible, 2012, as well as information on the distribution of the carry forward for 2011-2012; whether the budget envelope included the professional staff salary increment; whether gender was included in the policy or programme side of the budget; and, the basis of the efficiency ratio and how solid and reliable it was.

18. Management began by clarifying that this is a preliminary overview document with the intention of seeking approval for the overall envelope.
19. On policy dialogue, the committee was informed that this was an on-going effort and not necessarily related to the budget process. On the issue of one-time items, Management confirmed that there are none planned at this stage, thus explaining why that line was shown as zero. Regarding the differences in the numbers for the programme of loans and grants between the high-level preview presented in 2011 and the current document, a more detailed analysis of the two documents would have to be undertaken and Management would revert at a later stage. On the regional allocation of the programme of loans and grants, Management clarified that the allocations were actually country-based and established in accordance with the Performance-based Allocation System (PBAS), which takes into account such factors as GNI per capita, rural population size and performance. Regarding the query on thematic issues, it was highlighted that the apparent discrepancy between the current document and the Strategic Framework arose due mainly to measurability – while the Strategic Framework was setting objectives for work, the current document was outlining a measurable, results-based programme of work and the objectives of the two categories would be found in several of the thematic areas included. It should be noted that all lending activities are covered within the six thematic areas quite aside the Strategic Framework. On IFAD8 geographical distribution, the RIDE report captures that. On the regional distribution, besides the PBAS already referred to, Management further clarified that IFAD has agreed to a safeguard of not less than 40 per cent of the entire programme of loans and grants to sub-Saharan Africa.
20. The Committee was informed that the programme of loans and grants presented in the report is one based on IFAD's regular resources and is flat. Some projected reflows may not necessarily be so certain and linear.
21. Management also mentioned their efficiency programme is aimed at trying to do certain things at less cost.
22. Recalling the requests made for the provision of further information on actuals, Management clarified that a separate document providing such information was being prepared and would be made available for the upcoming session of the Executive Board, in order to aid consideration of the high-level preview.
23. On the carry forward issue, Management explained that Financial Regulations allow a 3 per cent carry forward, and in 2011 with a 96 per cent utilization, it was possible to have a 3 per cent carry over. The issue of the salary increase for the professionals has been handled in the same manner as last year, in that if the increment does not come through, the funds will not be spent. Regarding gender, Management underlined that gender was of course mainstreamed into both programmes as well as the organization as a whole, but it was explained that the budget did not contain a specific line for this topic. With regard to Supplementary funds, due to the unpredictable nature of their flows, ongoing costs are captured under the administrative budget.

24. The Committee was further informed that there would be a 0.12 per cent no gain no loss adjustment to the professional salary component to be taken to the General Assembly for approval by the ICSC.
25. With regard to some members' requests for clarification on the maintenance of the services provided to IFAD's Governing Bodies, Management highlighted that a specific proposal was being presented to the upcoming session of the Board. In this regard and in light of the continued necessity for budgetary prudence and increased savings, a number of cost-cutting measures were being envisaged and would be discussed with the Executive Board. Among these is, inter alia, the introduction of a cap on document length in order to ensure that key information continues to be provided in all of IFAD's languages.
26. Comments for the IOE component included a request for an opportunity to review the final report of the CLE Efficiency in an informal seminar prior to Board discussion; whether the final budget presented in December is expected to be different from the current preview; clarification on the link between narrative and figures; where consultancy costs fit in the budget and clarification on the role of IOE in impact evaluation and cost implications thereof and whether IOE could inform the Committee if other MDBs review Project Completion Reports (PCR) 100 per cent, considering the implication for IOE work load given the possibility of a rapid increase in the number of PCRs provided by IFAD Management.
27. In responding, IOE noted some convergence in the type of comments they received from the Audit Committee as well as those received at the Evaluation Committee meeting.
28. The committee was informed of the progress of the corporate-level evaluation on efficiency that is currently planned for presentation to the December Executive Board. An update on the process of the evaluation as well as a final proposal on date for Board submission depending on the progress would be presented to the October Evaluation Committee session. In the meantime, an interim report has been issued to IFAD Management at the end of July for their comments, which are expected by the end of September 2012. IOE also agreed to organize an informal seminar before the final report is presented to the Executive Board to discuss the main findings and recommendations of the evaluation.
29. The committee was informed that the extent to which the final budget will be different from the preview will largely depend on the final list of evaluations whose development is currently underway. Major changes are not expected. IOE reiterated that they are part of the debate on impact evaluation in IFAD and that IOE is planning to assist IFAD in developing capacity for undertaking impact evaluations. IOE further outlined ways in which they are already moving to getting more involved on impact evaluations.
30. On Consultancy costs, the committee was informed that the costs are largely embedded within the line for non-staff costs. The final budget proposal will provide more information on consultancy costs.
31. On the validations for PCRs, IOE responded that it would depend on the number of PCRs that will actually be completed by Governments/IFAD Management. So far, IOE typically undertake 10 to 25 validations in a year depending on how many PCRs are completed in any given year. It is envisaged that there might be around 30 PCRs in 2013. IOE resources and the timing of the delivery of PCRs from IFAD Management to IOE will impact on how many PCRs are actually validated. In case less than a hundred per

cent of the PCRs are validated, then a statistically representative sample will be selected, using random sampling as per ECG Good Practice Standards.

32. The Chairperson summed up the item and stated that the Committee took note of the administrative budget. The Chairperson also recalled the additional information requested by the Committee and the assurances given by Management that this would be provided in time for the Executive Board's consideration of the document. The Audit Committee agreed with the level of the proposal of the IOE budget but also noted that some issues remained to be addressed either at the Board or at the next Evaluation Committee, prior to the Audit Committee's consideration of the final proposal in November.

Progress report on the work plan of the IFAD Office of Audit and Oversight for 2012

33. The chairperson introduced the item and invited Management to present the item.
34. Management informed the Committee that the report is a summary of the work plan implementation for 2012 as follows:
35. **Audit:** The approved work plan is on course to being completed. The audits of project design process, country office support services, and Held to Maturity portfolio have been completed. There are no significant changes to report or propose.
36. **Investigations:** The rate of receipt of complaints is in line with that of last year. A staffing disruption was encountered with the resignation of the Investigation Officer in March but was addressed by the recruitment of a new Investigation officer in July. Additional resources were provided through budgetary reallocation.
37. The rate of implementation of recommendations is considered very good.
38. The Audit Committee was updated on the progress regarding the external quality assurance review of the internal audit function. The President has endorsed the option of a full external independent assessment and has appointed the Director of his Office to oversee the selection process for an assessor which is being managed by the IFAD Procurement Office using IFAD procurement procedures. The assessment will be conducted in the period October to November 2012. The final report is expected to be issued within 2012 and will be presented to the Audit Committee at its first meeting in 2013. In the course of the assessment the views of the Committee will need to be considered and in this regard the assessors will be contacting the Chair and possibly some members of the Committee in the next month for interviews.
39. Comments for Management included clarifications on the exact amounts involved in budget reallocations; clarification on the status of certain audits like the efficiency of the Legal System, in-country assessments and status and clarification on the capacity building initiative.
40. On the budget reallocations, Management clarified that the amount involved was approximately US\$200,000, which came from budgetary reallocation during the mid-year review. It was used on investigations consultants. On the audits, it was clarified that the audit of legal services is yet to commence. For country audits, countries are identified based on risk considerations. The Committee was informed that AUO had intended to undertake two capacity building assessments but one had to be put on hold following re-evaluation of need, the other one is likely to be conducted once funds are sourced.

41. The Audit Committee took note of the report.

Standard financial reports presented to the Executive Board

42. The Chairperson introduced the items and informed the committee that there were a number of reports to be discussed under this item namely, Report on the Ninth Replenishment of IFAD resources; the status of the Eighth Replenishment, Resources available for commitment; Report on IFAD's investment portfolio for the second quarter of 2012 and status of arrears in principal, interest and service charge payments.
43. Comments from members included clarification on the composition of the 85 per cent of the Ninth Replenishment target as well as the date from which it takes effect; and, whether the level of pledges include all numbers in the footnotes. Welcoming the US\$30million payment to the Eighth Replenishment made by the USA at the end of July, the Committee noted that this was not reflected in the status report of the Eighth Replenishment which showed the status as at end June 2012.
44. Management clarified that the 85 per cent is part of IFAD's regulations and is calculated on the Replenishment target. The Amount making up the 85 per cent includes all replenishment pledges translated to US dollars using a replenishment fixed rate of exchange, pledges may take various forms from written to oral. The footnotes include clarifications on pledges, some of which come with conditions such as parliamentary ratifications. All pledges are cleared by IFAD's Legal Counsel before inclusion as counting towards pledges to be included to be measured against the target.
45. Management further clarified that the Eighth Replenishment status report had a cut-off date of 30th June and did not include payments made subsequent to that but a note would be added for the Report to the Board; the US Funds had indeed been received.
46. There were no further comments on the rest of the reports.

Consultancy management procedures

47. The Chairperson reminded the committee the item had been postponed to the November session.

Update on the costs and financial implications in relation to the recent changes in the housing arrangement for the Global Mechanism of the United Nations Convention to Combat Desertification

48. The chairperson introduced the item and invited Management to present the item.
49. Management informed the committee of the changes as a result of the revised memorandum of understanding between IFAD and UNCCD which would limit the housing arrangement to provision of office space. The estimated future costs are approximately US\$210,000, representing US\$160,000 for administrative costs and US\$50,000 for ICT.
50. The above cost estimates are based on work force of 25 staff and consultants and does not include Legal, HR, protocol, finance and corporate costs. These excluded services cost approximately USD490,000.
51. The 2012 IFAD Management fees amount to USD186,000; 8 per cent of the administrative budget.
52. The Committee was also informed of the underfunding of the GM administrative budget which is now being covered by month by month transfers from UNCCD.

53. Comments from members included clarification on the amount needed to fund the budget for the remaining part of the year; status of the liquidity of UNCCD and the number of legal cases which might have financial implications and their likely outcome.
54. Management responded that about US\$700,000 is required to meet the total approved budget shortfall to the end of the year. Management indicated that they are in constant touch with UNCCD alerting them of the funding gap and the need to finance it as soon as possible. On the issue of liquidity Management indicated that their understanding was it depended on UNCCD receiving funds from their donors.
55. On the number of legal cases, Management indicated that three cases, all involving GS staff, are under review in consultation with an external Counsel.
56. The update was noted.

Oral update on the sustainable cash flow approach

57. Management was invited to present the oral update on the sustainable cash flow (SCF) approach.
58. The presentation covered sustainable cash flow approach for determination of the programme of loans and grants; main assumptions and flows underlying the SCF model; examples of model impacts with changing assumptions; implementation and monitoring of the initiative.
59. The members were informed of the decision to move from the Advance Commitment Authority (ACA) approach to SCF during the 9th Replenishment consultations. The advantages of the SCF over ACA were highlighted.
60. The rationale of the SCF model for PoLG determination and underlying assumption including the fact that it accounts for all cash inflows and outflows. The Committee was reminded of the importance of maintaining solid assumptions which need to be reviewed and revised as appropriate.
61. Management also presented examples of the impact on the financial model of changes in various key assumptions.
62. Management concluded by stating that there would be one base model to be updated with Financial statements actuals, variable assumptions would be updated on parallel models and regular updates would be provided to the Audit Committee and Internal Finance Committee.
63. Comments from Committee members included stating that the committee needs to form an opinion on the viability of the system which seems to be the way forward; the frequency of reporting to the Committee and whether the SCF will supersede the ACA.
64. Management confirmed that it was agreed as part of the replenishment to phase out ACA. Status of the SCF will be updated and reported to the Audit Committee and the Executive Board probably twice a year.
65. The update was noted.

Oral update on the development of the Loans and Grants System

66. Management presented an oral update on the project and informed the Committee of the following key areas and highlights:
67. The latest version of the functional side of the LGS, Flexcube will be installed. An increase in the number of customizations led to an amendment in the contract with a slight increase in the cost, within the contingency budget.

68. Management reiterated IFAD's intention to modify certain procedures in the area of billing and back dated adjustments of fund flows to minimize customizations and that there were no significant delays in the current activities although a slight increase in the project timeline for phase 1 is envisaged.
69. Management informed the committee that there might be some slight increase in project costs from the Data warehouse side of the project as the initial cost estimates were too low. The Committee was informed of the current activities for both the functional and the Data warehouse side of the project, both of which appear on course; as well as envisaged next steps. The only project key risk identified is data migration and is being monitored closely.
70. The Chairperson thanked Management for the update. Upon request of the Chairperson, a written copy of the oral presentation was distributed to the Committee. There were no comments from members.
71. The update was noted.

Other Business – Report of the Joint Inspections Unit (JIU):Accountability Frameworks in the United Nations System

72. The Chairperson introduced the item and informed the committee that he had requested the inclusion of this item on the agenda in order to review and get a sense of how IFAD, as an organization, deals with the culture of transparency and accountability. This is with a view to hearing from Management as to how they apply accountability in the organization. The other Rome-based UN agencies have taken the report on board and are adopting its elements and recommendations.
73. Management, through the Legal Counsel, clarified that all the questions are taken care of in the IFAD structure and governance. The key elements of Political covenants, financial management and administration and internal controls are addressed within the existing framework of governance and structure of IFAD as follows:
 - Political covenants are guided by the Agreement Establishing IFAD which functions as a constitution and shows the structure and governance of the Fund; guides policy setting and criteria including evaluation policy.
 - Financial Management and administration is guided by the Financial Regulations, Executive Board decisions and the Human Resources Policy.
 - Internal Controls are enshrined in the functions as was explained by the Internal Audit. These are as required by the Financial regulations set up by the Governing Council and are assessed on a regular basis by the Executive Board.
74. The Committee was informed that Management is open to review the report for possible opportunities for improvement but this was an overview of elements already in place in IFAD.
75. The Chair appreciated the response and suggested a review be done with a view to identifying areas for improvement. An update on status of this review would be appreciated at the Committee's next meeting.

Other Business - Other

76. A member raised an issue on whether further information about the Global Mechanism could be provided in the form of a paper to be distributed to the Committee.
77. Management reminded the Committee that the President would be reporting orally on this issue at the upcoming Executive Board session.
78. The Chairperson summed up the issue stating that the Audit Committee was only addressing the financial elements of the matter and a wider discussion could be considered in another forum such as the Convenors and Friends.