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Report of the Chairperson on the 140th meeting of the Audit Committee

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Executive Board — 118th Session
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For: Review

Report of the Chairperson on the 140th meeting of the Audit Committee

1. The Audit Committee wishes to bring to the attention of the Executive Board the matters examined at the 140th meeting of the Committee held on 4 July 2016.
Adoption of the agenda
2. The agenda was adopted, noting that, under other business, Management would provide an update on progress on the following topics:
 - Ñ Implementation of the Loans and Grants System 2 (LGS 2); and
 - Ñ IFAD's approach to corporate planning and budgeting: moving from results clusters to results pillars.
3. The Chairperson of the Audit Committee advised that, due to an apparent conflict of interest, he wished to recuse himself from deliberations on items 4, 5 and 6. The Committee agreed that the representative for Germany, Ms Martina Metz, would take the Chair for consideration of these items.
4. Before proceeding with the meeting, the Vice-President of IFAD took the floor to make some opening remarks. The Committee was informed that the Vice-President acts as Interim Head, Financial Operations Department (FOD), while steps are being taken to hire an Interim Associate Vice-President, Chief Financial Officer and Chief Controller. The definitive hiring process will be expedited in 2017 under the new Presidency. Information was also provided on the measures taken to further strengthen FOD through the realignment and redistribution of the responsibilities and duties of the Controller's and Financial Services (CFS) Division in two new divisions: (i) the Accounting and Controller's Division (ACD); and (ii) the Financial Management Services Division (FMD). This organizational change is taking place gradually, is budget-neutral and will be completed at the latest by end-September 2016. The Vice-President provided an update on steps taken so far in implementing the International Financial Reporting Standard 9 (IFRS 9). It was noted that IFAD acted speedily to tighten security on its access points to SWIFT, following a number of serious cyberattacks affecting the SWIFT global bank payment system.
5. The Vice-President stated that three notes would be presented at the Audit Committee meeting and Executive Board session in September: (i) to provide information on the fixing of the interest rate; (ii) to propose measures to protect the institution against the risks of negative interest rates; and (iii) to propose access to the last tranche of EUR 100 million under the current KfW Development Bank (KfW) Framework Agreement.
Minutes of the 139th meeting of the Audit Committee
6. The minutes were approved without comment.
External auditor's report on internal control and accounting procedures
7. The external auditors, Deloitte & Touche, presented the internal control and accounting procedures report, stating that the recommendations included had arisen during the course of the audit for the year ended 31 December 2015. None of the recommendations had given rise to a qualification of either their audit opinion on the consolidated financial statements or Management's assertion report regarding the effectiveness of internal controls over financial reporting.
8. During the audit, improvements were noted in follow-up on the prior year's recommendations. During the 2015 audit, one issue of high priority had been identified in relation to the Treasury Services Division (TRE) and, in particular, to the enhancement of internal policies on internal investment activities and improvements to the Treasury database. It was also noted that Management had already undertaken proactive measures to implement this recommendation.

9. The document was reviewed and Audit Committee members had no major observations.

External Auditor's audit strategy memorandum for the year ending 31 December 2016
10. In presenting the strategy memorandum, the audit partner thanked Management for the assistance and cooperation provided during the planning exercise. He informed the Committee that, in line with the prior year, four key audit risks had been identified for the audit of the 2016 accounts: fair value calculation on loans; foreign currency translation as a matter of standard procedure; revenue recognition; and Management override, with a focus on Management judgement or estimation.
11. The document was considered reviewed.

Award of external auditor contract for 2017-2021
12. Management provided an oral update on the selection process for the external auditor for the contract period covering the consolidated financial statements 2017-2021.
13. It was noted that, in May 2016, Management expedited the selection process as endorsed by the Audit Committee and in accordance with the tentative timetable presented during the 139th meeting. Following submission of an expression of interest, qualified audit firms were invited to participate in the tender process. Offers submitted were scrutinized by a technical evaluation committee and by a separate commercial committee.
14. As part of the technical evaluation, each audit firm delivered a presentation, which was attended by Ms Martina Metz, representative for Germany. The final evaluation report, summarizing the commercial and technical evaluations, was to be presented to the Contract Review Committee on 7 July 2016. Mr Nicholas Strychacz, representative for the United States, would participate as an observer.
15. The final results, as well as a detailed report on the selection process, will be presented at the Audit Committee meeting in September 2016, with the aim of receiving final approval prior to the Executive Board session of December 2016.
16. The Committee took note of the update with no comments.

Procedure for drafting, clearance and sharing of records of Audit Committee meetings
17. In response to the request of the Audit Committee at its 139th meeting, the Office of the Secretary prepared and presented a document providing an overview of the recently approved procedures for drafting, clearance and sharing of records of Evaluation Committee sessions, which also included a study on whether similar procedures could be applicable also to the Audit Committee. In presenting the document, Management highlighted the main procedural differences between the Evaluation and Audit Committees. In doing so, the confidential nature of Audit Committee documents was noted and the Committee was reminded that, in accordance with the IFAD Policy on the Disclosure of Documents (2010), Audit Committee documents and minutes remain restricted to the Audit Committee only. The report of the Audit Committee Chairperson on the other hand, is made public, as it is presented to the Executive Board.
18. The following options were presented:
 - (i) Maintaining the two reporting lines currently in place: the Chairperson's report for the review of the Board, and the minutes for distribution to Audit Committee members; or
 - (ii) Maintaining the two reporting lines and, in addition, sharing the draft Chairperson's report with Audit Committee members for comments before

finalizing it for submission to the Board. However, it was noted that this option might seriously delay the clearance process and increase the risk of late dispatch to Board representatives, due to the proximity of timing of Audit Committee meetings and Board sessions.

19. Finally, it was underlined that any changes to the current reporting arrangements may require amendment of the existing rules and, accordingly, approval by the Executive Board.
20. In analysing these options, upon the proposal of the Chair, members agreed that the two reporting lines would be maintained and the Chairperson's report would be circulated before its finalization for the Executive Board in order to receive comments and feedback from members (option 2), with the understanding that ultimate responsibility for the finalization of the paper will rest with the Chairperson. This procedure would be in place during the current Chairpersonship. However, the deadline for submission of feedback would be set at each meeting, and the Committee was reminded that the deadline would often be tight, due to the frequent proximity of Board sessions and Audit Committee meetings.

Proposed dates for meetings of the Audit Committee in 2017

21. The Committee was presented with a list of proposed dates for meetings of the Audit Committee in 2017 and was informed that the dates were identified well in advance to avoid scheduling conflicts with the increasing number of events organized by the Rome-based agencies.
 22. In this respect, one member requested that more details be provided of meetings and events on the Rome-based agencies' common calendar. The Committee was informed that FAO was in charge of keeping the calendar up-to-date and they would be contacted to request that all details of the meetings be provided.
 23. The proposed dates were approved by the Committee.
- Standard financial reports presented to the Executive Board
24. Management presented the report on IFAD's investment portfolio for the first quarter of 2016 for Audit Committee review.
 25. The Director and Treasurer, TRE, introduced the document, highlighting that the investment portfolio had a very good performance at the start of 2016, recording a 1.59 per cent net rate of return, which translated into investment income of US\$24.4 million, net of all investment-related fees.
 26. The determinants of this performance were a strong rebound in global markets, sparked by the change in sentiment following the market perception that the United States Federal Reserve might follow a slower than anticipated pattern in raising interest rates. This positive reaction affected all asset classes, both risky and defensive.
 27. The Director and Treasurer provided a preliminary estimate of the performance of the portfolio as of 27 June. This captured most of the very pronounced market reaction to the results of the referendum in the United Kingdom on its leaving the European Union, which took place on 23 June.
 28. No negative impact on IFAD's portfolio of material size was measured following the trading sessions on 24 and 27 June. Preliminary indications suggest that the rate of return of IFAD's portfolio for the first half of 2016 may be on the order of 2.5 per cent net of fees, with a return in June month-to-date of about half a per cent – a very positive performance indeed in the face of highly unsettled global markets.
 29. During the discussion, it was noted that the portfolio had also performed well versus benchmarks. Concerning currency misalignment versus the special drawing right (SDR), it was suggested that IFAD might consult other international financial

institutions (IFIs), in particular the World Bank. The Director and Treasurer explained that talks are being held with the World Bank that may result soon in stronger cooperation on portfolio management.

30. The report was considered reviewed.

Other business

31. Under other business, Management provided an oral update on the progress of the implementation of LGS 2, now renamed "the IFAD Client Portal (ICP)". The ICP will provide facilities for direct submission of withdrawal applications and analytics, allowing faster turnaround and accurate information. This change will ensure that IFAD is an effective and efficient organization focused on clients' needs. The principal business driver for this project is to improve client experience in doing business with IFAD. In fact, the main benefits and efficiencies of ICP accrue to the borrower/recipient of IFAD financing: improved service delivery, reduced cycle times and better visibility and access to data.
32. It was noted that the procurement process for the selection of a vendor to deliver the portal solution was completed in the fourth quarter 2015, and in December 2015 Senior Management approved the scope and budget of the project.
33. The scope foresees a more comprehensive platform than had been envisaged in 2011: additional functionality has been included to address more closely stakeholders' requests, as contained in a related survey that IFAD carried out in 2015.
34. In line with related discussions in the Executive Board, Senior Management decided to ensure full design and to roll out the portal in all the IFAD official languages: Arabic, English, French and Spanish.
35. The platform will incorporate state-of-the-art security and best practice processes to mitigate the risk of possible cyberattacks.
36. Due to the complexity of implementation, a phased approach has been adopted for the release of functionality, with the originally planned electronic disbursement process and reporting included in Phase A. Phase B concerns the roll out of language versions, and Phase C the additional functionality relating to operational work.
37. The project kick-off took place on 29 February 2016. The testing phase is scheduled to start in September and will be concluded with the deployment of the solution to permit electronic disbursements by a first wave of borrowers/recipients in December 2016. These borrowers will be identified based on criteria for readiness and technological maturity as part of the roll out strategy.
38. The project time line for Phase A is 12 months, although all efforts will be made to deliver the first set of functionality by December 2016. The implementation of phases B and C is expected to start in 2017.
39. Management provided a brief status update on "IFAD's approach to corporate planning and budgeting: moving from results clusters to results pillars", highlighting that this initiative aims to ensure that results are aligned even more closely with the new IFAD Strategic Framework 2016-2025.
40. It was noted that this exercise constitutes a review of how IFAD plans and organizes itself by increasing transparency and clarity: (i) deliverables planned by every group in IFAD; (ii) alignment between plans and IFAD priorities; (iii) the cost of planned deliverables; and (iv) budgets better linked to results and outputs. These improvements will allow IFAD to better analyse, monitor, manage and focus its resources on addressing its strategic priorities and delivering its planned outputs.

41. It was also noted that improvements will be introduced in a gradual and transitional manner during the 2018 annual planning and budgeting cycle.
42. The enhancements will entail creating a stronger focus on outputs and results. The main thrust of the reform will be to make planning for these work streams increasingly and consistently output-based, with each output having an associated budget, wherever possible based on a standard output unit cost.
43. Departments across IFAD are engaged in an exercise of defining institutional level outputs that their workflows generate, bearing in mind that new directions and priorities are consistent with the results pillars articulated in the IFAD Strategic Framework 2016-2025. The focus on “institutional level” outputs should produce a more-coherent, consistent, meaningful and manageable list of outputs. Audit Committee members were informed that progress updates will be contained in the high-level budget preview document and 2017 budget document to be presented to the Executive Board sessions in September and December, respectively.
44. No additional items were discussed under other business.