

Document: EB 2017/120/R.14
Agenda: 10(a)
Date: 7 April 2017
Distribution: Public
Original: English

E



Report of the Chairperson on the 143rd meeting of the Audit Committee

Note to Executive Board representatives

Focal points:

Technical questions:

Advit Nath
Director and Controller
Accounting and Controller's Division
Tel.: +39 06 5459 2829
e-mail: a.nath@ifad.org

Allegra Saitto
Chief
Financial Reporting and Corporate Fiduciary
Accounting and Controller's Division
Tel.: +39 06 5459 2405
e-mail: a.saitto@ifad.org

Dispatch of documentation:

William Skinner
Chief
Governing Bodies Office
Tel.: +39 06 5459 2974
e-mail: gb_office@ifad.org

Executive Board — 120th Session
Rome, 10-11 April 2017

For: Review

Report of the Chairperson on the 143rd meeting of the Audit Committee

1. The Audit Committee wishes to bring to the attention of the Executive Board the matters examined at the 143rd meeting of the Committee, held on 3 April 2017.

Adoption of the agenda

2. The agenda was adopted, including the following topics under "Other business":
 - Procedures related to the drafting and finalization of the Audit Committee Chairperson's report to the Executive Board;
 - Procedures related to requests for internal audit reports;
 - Review of some internal audit reports [closed session].

Minutes of the 142nd meeting of the Audit Committee

3. The minutes were approved without comments.

Consolidated financial statements of IFAD as at 31 December 2016 (including the Management assertion report and an independent external attestation on the effectiveness of internal controls over financial reporting)

4. Management introduced this agenda item by noting the external auditor's unqualified/clean audit opinion on the Consolidated Financial Statements of IFAD as at 31 December 2016. Management noted that, for fiscal year 2016, it confirmed the operational effectiveness of all key internal controls over financial reporting in the management assertion report, with an independent external attestation by IFAD's external auditors.
5. Management identified key factors affecting IFAD's financial position and reported results, emphasizing that the overall financial situation was sound, and that long-term viability was being monitored closely. Additional details were provided on foreign exchange volatility impacting the financial statements, as well as on the various currency-risk mitigation measures adopted by the Fund. It was noted that at the end of December 2016, IFAD's liquidity was above the minimum liquidity-policy requirement. The impact of Debt Sustainability Framework (DSF) expenses on IFAD's financial position, and the importance of DSF compensation from Member States to IFAD as a main consideration for long-term financial viability, were underscored. It was noted that the level of pledges required as DSF compensation will increase to US\$37.1 million during the Eleventh Replenishment of IFAD's Resources (IFAD11).
6. IFAD's external auditors provided a brief commentary on the main areas of focus during the 2016 audit, i.e. fair-value accounting for IFAD's loan portfolio, foreign exchange impact, and management assumptions for revenue recognition, which is a standard audit procedure.
7. Members commended IFAD Management for the high-quality and detailed financial statements and supporting appendices. Clarifications were sought on foreign-exchange volatility and its potential relevance, the level of operating expenses, and the level of the impairment allowance on loans outstanding.
8. Management provided the necessary clarifications. In particular, it emphasized that foreign-exchange unrealized losses stem from the re-translation of primarily special drawing rights (SDR) denominated assets into dollars for reporting purposes and tend to net out over time. Under the current financing model, IFAD mitigates currency risk by matching the currency denomination both for assets (investment funds and loan receivables) and for financing commitments (approved and undisbursed loans and grants).

9. The adoption of single-currency loans will reduce the accounting impact of foreign-exchange movements, as IFAD assets would be denominated in United States dollars. It was noted that IFAD had entered into its first International Swaps and Derivatives Association master agreement, which will enable it to pursue cross-currency swaps and hedge currency risks more proactively.
10. The Consolidated Financial Statements were reviewed by the Audit Committee and will be presented to the 120th session of the Executive Board for endorsement, prior to the Governing Council's formal approval in February 2018.

Annual Report on the Activities of the Office of Audit and Oversight during 2016

11. The Office of Audit and Oversight (AUO) presented the report, highlighting that the purpose of the document was to provide details of the Office's activities in 2016. The document included a substantial summary of each audit report issued in 2016 and gave detailed information on open recommendations. It also provided information on its investigation activities.
 12. In 2016 AUO's main objective was to ensure proper audit coverage of the IFAD Country Offices (ICOs). AUO issued a report on cross-cutting institutional issues arising from six ICO audits and audited a further six. The audits did not reveal any areas of unacceptably high risk to the delivery of key corporate objectives. In total, AUO issued 94 recommendations to address the risks noted in these ICO audits, 16 of which were of high priority. Steps taken included the issuance of a revised ICO handbook with guidance and tools addressing specific areas, and the delegation of budgetary authority to ICOs on a pilot basis.
 13. AUO noted that no high-priority recommendations were overdue at end 2016.
 14. In the investigation area, during 2016 AUO gave a timely and effective response to alleged wrongdoing, by completing investigations into 56 complaints during the year – a much higher closure rate than in previous years – and generally ensuring a prompt and effective conclusion to the issues in question.
 15. Anticorruption awareness outreach was intensified through AUO participation in regional and other events, including the pilot launch of an anticorruption e-learning module. The investigative and sanctions processes, and AUO investigation capacity, were strengthened through the issuance of revised procedures, the deployment of new forensic tools, and segregated physical and IT environments for the investigation section.
 16. AUO's close collaboration with the Rome-based agencies (RBAs) was noted, particularly the fact that AUO had hosted the annual coordination day for all staff of the RBA internal oversight offices, as well as a well-attended joint RBA training event.
 17. Committee members requested clarifications on the investigation process and on the assessment of relevance of cases, as well as on the project procurement audit.
 18. AUO provided all necessary explanations, including on levels of approvals of decisions within IFAD. It also noted that project procurement would be a key area of emphasis in 2017. The audits of ICOs and programmes would focus on procurement; and a cross-cutting summary report would be issued in early 2018, to include a follow-up on the findings of the AUO 2014 audit on the same topic.
 19. The report was deemed reviewed.
- Update of the Corporate Working Group on the Policies and Criteria for IFAD Financing and Terms
20. Management presented an overview of the progress made by the Corporate Working Group on the review of IFAD's products, terms and pricing; and it made a series of observations for both the short and the medium terms, to be considered

by Senior Management. Work is under way to prioritize individual recommendations and agree the way forward for various topics, including the DSF, new products, considerations on pricing and the full-financial-cost-recovery principle, creation of a special reserve, single-currency lending and the conversion of SDR legacy loans into hard currency (dollar or euro). Management also noted that the evolving/exploratory nature of the borrowing discussions and other replenishment topics would influence the working group's activities and processes.

21. It was stressed that the DSF was a key element for the Fund's future viability. Management has undertaken a full review of DSF compensation mechanisms, and a document with some options will be presented to a future governing body session, particularly in the context of the IFAD11 consultations.
22. Management clarified that guarantees had been reviewed as a possible new instrument. It was also noted that there was interest from members in the underlying principles noted in the presentation, including that there should be no product-category cross-subsidization, and that work on the special reserve – in the light of enhanced borrowing activities – was still at a preliminary stage.
23. The overview was noted; the Committee asked Management to keep it abreast of significant developments, as these issues were of the utmost importance for the Fund.

Standard financial reports presented to the Executive Board

24. Management presented the following five reports for review by the Audit Committee:
 - Report on the status of contributions to the Tenth Replenishment of IFAD's Resources;
 - Report on IFAD's investment portfolio for 2016;
 - Status report on arrears in principal, interest and service-charge payments;
 - Estimated principal and net service charge payments forgone as a result of the implementation of the Debt Sustainability Framework;
 - Requirements for the thirty-eighth drawdown of Member States' contributions in 2017.
 25. Management provided an update on the status of IFAD10 and on the investment portfolio performance.
 26. Management updated Audit Committee members on the latest portfolio developments, highlighting the positive performance recorded in 2016 and the significant divestments executed from the emerging markets and global inflation-indexed bond portfolios. Management also provided an estimated performance for the first quarter in 2017 in the region of 0.44 basis points.
 27. The Committee reviewed the draw-down requirements for 2017, which will be presented to the 120th session of the Executive Board for approval.
 28. The reports were deemed reviewed.
- Other business
29. Three sub-items were considered by the Committee under "Other business".
 - (a) Procedures related to the drafting and finalization of the Audit Committee Chairperson's report to the Executive Board
 30. The Chairperson reminded the Committee that, pursuant to the decision that had been taken at the 140th meeting, Chairperson's reports were typically circulated for comments and feedback from members prior to finalization for the Executive Board. The Chairperson stated that he intended to continue the same practice; but, on an exceptional basis, the report for this meeting would not be circulated for

feedback, owing to the proximity of the Audit Committee meeting and the Executive Board session. The practice will be reconsidered at the 144th meeting of the Audit Committee.

(b) Procedures related to requests for internal audit reports

31. It is a prerogative of Audit Committee members to request access and discussion on internal audit reports. The Chairperson proposed, and the Committee agreed, that any Audit Committee member who wanted an internal audit report to be included on the agenda for discussion, should notify the Chair at least one week in advance, indicating the main aspects of the reports that they wished to discuss. This would give time for the Director, AUO, to prepare adequately to address the issues in question.

(c) Review of some internal audit reports

32. The Audit Committee held a closed session with AUO to review a number of internal audit reports.