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## **Report of the Chairperson on the 160<sup>th</sup> Meeting of the Audit Committee**

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Executive Board — 132<sup>nd</sup> Session  
Rome, 19-21 April 2021

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**For: Information**

## **Executive summary**

1. In light of the COVID-19 pandemic, the 160<sup>th</sup> meeting of the Audit Committee was held remotely.
2. The Audit Committee discussed a large number of documents, most of which would be presented to the Executive Board for review or approval at its 132<sup>nd</sup> session. Items included the following:
  - Requirements for the forty-second drawdown of Member States' contributions in 2021;
  - Review of the Consolidated Financial Statements of IFAD as at 31 December 2020, including the Management assertion report and an independent external attestation on the effectiveness of internal controls over financial reporting;
  - Annual review of the activities of the Office of Audit and Oversight;
  - Topics related to the IFAD12 business model and financial framework (2022-2024) – for review:
    - (a) Borrowed Resource Access Mechanism (AC 2021/160/R.7 + Add.1)
    - (b) Update to IFAD's financing conditions (AC 2021/160/R.8 + Add.1 + Add.2)
  - Update on the usage of carry-forward funds.

## **Report of the Chairperson on the 160<sup>th</sup> meeting of the Audit Committee**

1. The Audit Committee wishes to bring to the attention of the Executive Board the matters examined at the 160<sup>th</sup> meeting of the Committee held on 7 April 2021. In light of the COVID-19 emergency, the meeting was held remotely through Zoom videoconferencing.

### **Adoption of the agenda**

2. The agenda was adopted with no changes.

### **Minutes of the 159<sup>th</sup> meeting**

3. The minutes were approved with some changes proposed by Committee members.

### **Plan for the selection of the external auditor 2022-2026 (AC 2021/160/R.10) – for information**

4. Management noted that in line with the IFAD policy on rotation and on services to be provided by the external auditor, Deloitte & Touche SpA would end its second mandate with the audit of the 2021 financial statements. Management provided an overview of the selection process of the new external audit firm for a mandate covering the period 2022 to 2026 inclusive.
5. The document was reviewed. It was noted that the selection process would be supported by the United Kingdom acting as the Audit Committee focal point, while the Chair, committing himself to also follow the process, encouraged other Committee members to do the same as well on a best effort basis.

### **Requirements for the forty-second drawdown of Member States' contributions in 2021 (AC 2021/160/R.11) – for review**

6. Management introduced the agenda item noting drawdown requirements for fiscal year 2021, in line with the latest resources available for commitment and projected disbursements. The document was reviewed by Committee members and would be submitted at the forthcoming session of the Executive Board for approval.

### **Standard financial reports presented to the Executive Board – for review**

#### **(a) Report on IFAD's Investment Portfolio for 2020 (AC 2021/160/R.13)**

#### **(d) Report on the Status of Contributions to the Twelfth Replenishment of IFAD's Resources (AC 2021/160/R.16)**

7. Management provided an overview of the investment portfolio's performance for fiscal year 2020, which was affected by COVID-related volatility, and provided an update on the status of the Twelfth Replenishment of IFAD's Resources (IFAD12).
8. The Committee reviewed the documents, both of which would be submitted to the forthcoming session of the Executive Board for information.

### **Draft provisional agenda for the 161<sup>st</sup> Meeting of the Audit Committee: (AC 2021/160/R.12) – for review**

9. The Committee reviewed and adopted the agenda for the 161<sup>st</sup> meeting, noting that the meeting would be held on 28 June 2021.

### **Other business**

#### **(a) Update on the proposal to enter into a borrowing arrangement with the Department of Foreign Affairs, Trade and Development of Canada to support the IFAD11 programme of loans and grants**

10. Management provided an oral update of the borrowing arrangements recently agreed with the Department of Foreign Affairs, Trade and Development of Canada.

It was noted that the loan had already been approved via vote by correspondence by the Executive Board on 5 March 2021.

11. The Committee noted the update.

**(b) Increasing Transparency for Greater Accountability Action Plan**

12. The Office of Audit and Oversight (AUO) provided an oral update on the Increasing Transparency for Greater Accountability Action Plan, approved in December 2017. The Operational Policy and Results Division (OPR) had been monitoring the progress made in the implementation of IFAD11 commitments, including commitment 42, which was now fully operational. AUO had already concluded that all 22 initiatives listed in the action plan had been substantially implemented before 2020 and, accordingly, with the agreement of Management, did not produce a progress report for 2020 considering that the benefit of a further progress report was limited. AUO would consider including a final assessment of the Action Plan in its workplan for 2022. OPR presented an update of the actions that are ongoing.
13. Committee members requested clarification as to the possibility of supporting governments with grants to ensure more transparency in publishing data, as well as on the implementation of the framework for operational feedback from stakeholders. Committee members also asked about the possibility of timely posting of internal audit reports on the Member States Interactive Platform.
14. Management informed the Committee about grants being provided to enhance governments' capacity in results-based management, including communication on results and outcomes. AUO also clarified that internal audit reports were published in accordance with current procedures. Given the Committee's request that such reports be made available to Committee members at an early stage, AUO will coordinate with the Chair to ensure that this is applied going forward. If needed, the AUO Charter would be amended to reflect this procedure.
15. The update was noted.

**IFAD financial statements – for review**

**(a) Review of the Consolidated Financial Statements of IFAD as at 31 December 2020, including the Management assertion report and an independent external attestation on the effectiveness of internal controls over financial reporting (including a closed session with the external auditor, if required)  
(AC 2021/160/R.3 + Add.1 + Add.2 + Add.3)**

**(b) High-level Review of the IFAD-only Financial Statements for 2020  
(AC 2021/160/R.4)**

16. Management introduced this agenda item, noting the external auditor's unqualified/clean audit opinion on the Consolidated Financial Statements of IFAD as at 31 December 2020. For fiscal year 2020, Management confirmed the operational effectiveness of all key internal controls over financial reporting in the Management assertion report, with an independent attestation by IFAD's external auditor.
17. Management identified the 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. It was noted that at the end of December 2020, all financial ratios were within IFAD policy thresholds and that liquidity was above the minimum liquidity requirement. The external auditor provided details about audit activities and additional tests/assessments performed in light of the potential risks posed by the COVID-19 pandemic.
18. Committee members requested information on some trends and assumptions, and clarification about possible impacts of the rating process on the preparation of the financial statements.

19. Management provided the necessary details. The external auditor clarified that the preparation of financial statements was compliant with industry standards and had not been impacted by the rating process.
20. The Consolidated Financial Statements were deemed reviewed and would be presented to the 132<sup>nd</sup> session of the Executive Board for endorsement, prior to the Governing Council's formal approval in February 2022.

**Annual Report on the Activities of the Office of Audit and Oversight (AUO) during 2020 and review of the adequacy of the internal oversight mechanisms (AC 2021/160/R.5) – for review**

21. AUO presented the report on internal audit and investigation activities in 2020. AUO highlighted that IFAD's substantial organizational, financial, workforce and business reforms had continued in 2020, putting pressure on staff capacity as well as on the control environment. It was noted that the COVID-19 pandemic had exacerbated the challenges and that IFAD had put in place a wide range of timely measures which mitigated any adverse impact.
22. AUO's audit work on hubs, country programmes, information and communications technology, security processes, fraud risk management and financial controls revealed generally good compliance with controls and institutional decisions. There was no indication that the operational risks associated with the ongoing changes or the pandemic were materializing in any significant way.
23. AUO's limited audit work on country programmes pointed to the need to further strengthen IFAD's supervision of project procurement and contract management activities. AUO noted that there were clear indications of significant strengthening of IFAD's financial architecture in 2020. AUO also stated that the assignment of a AA+ public credit rating by two rating agencies in the latter part of the year demonstrated the significant progress achieved in this area and the solid management of financial risks.
24. The high intake of project-related corruption allegations, a trend that began in 2018, had continued in 2020, notwithstanding the operational activity slow down due to the pandemic.
25. In 2020, AUO had faced capacity challenges due to significant turnover in staff and consultants and the participation of four staff members in the time-intensive IFAD reassignment process. AUO also updated the Committee on its budget and the allocation by Management of the additional resources requested to meet its needs for the year. AUO further informed the Committee that both recommendations pertaining to the Benin country programme had now been implemented.
26. Committee members noted that programme delivery and procurement were recurrent issues and that implementing the ongoing reforms during such a challenging period had stressed the control environment. The Committee requested details about: the timing of the required external quality assessment (EQA) of the audit function; measures taken to safeguard AUO business continuity given the ongoing staffing changes and to ensure adequate coverage of risks identified (such as increased cyber risks); the sharing within IFAD of fraud/corruption-related findings for prevention and risk mitigation; and the apparent slowdown in the implementation of audit recommendations.
27. AUO noted that EQAs are routinely conducted every five years and that considering the robust annual self-assessment process under the quality assurance and improvement programme, it did not see a need to bring forward the timing of the next EQA. In terms of business continuity, it was noted that the division had mature, stable and comprehensive procedures in place and a thorough handover process, therefore no significant disruptions were foreseen as a result of the transition. All remedies for Benin and Nigeria had been implemented; the slow

down experienced in implementing recommendations was mainly due to the need to ensure alignment with ongoing business process review reforms. The IFAD Executive Management Committee was closely monitoring implementation progress. AUO informed members that it shared information from investigations systematically with Management to facilitate risk mitigation. Management highlighted the role of quarterly meetings between AUO and all concerned departments/divisions (Programme Management Department, Financial Management Services Division, and Financial Controller's Division) in ensuring the effective mitigation of fraud and corruption risk.

28. The document was deemed as reviewed.

**Update on the usage of carry-forward funds (AC 2021/160/R.6) – for review**

29. Management provided an update on the usage of carry-forward funds noting that that the total balance carried forward from 2020 to 2021 was US\$15.48 million. The Committee was informed that approximately 17.8 per cent of funds had been allocated and utilized.
30. Committee members requested some clarifications about liaison offices, the applied apportionment principles for the 2020 carry-forward funds, potential cross-subsidization of activities through the use of carry forward and an update on how IFAD is addressing current audit recommendations.
31. Committee members also reiterated that continued regular updates on the utilization of carry-forward funds were much appreciated and that such funds should not be used to cover recurrent costs.
32. Management clarified that strict apportionment principles were applied to ensure that only one-off activities were funded from carry-forward funds. A system had been set up to avoid cross-subsidization. It was further specified that the main areas for which the carry forward was used related to challenges deriving from COVID (e.g. to ensure physical and cyber security) and Decentralization 2.0.
33. Management confirmed that the next update on the use of carry-forward funds would be delivered as planned in September.
34. The update was noted and would be submitted to the forthcoming session of the Executive Board.

**Topics related to the IFAD12 business model and financial framework (2022-2024) – for review:**

**(a) Borrowed Resource Access Mechanism (AC 2021/160/R.7 + Add.1)**

**(b) Update to IFAD's financing conditions (AC 2021/160/R.8 + Add.1 + Add.2)**

35. Management introduced the agenda items highlighting that both documents had been elaborated in parallel, based on the conversations held within the Executive Board Working Group on the Performance-Based Allocation System (PBAS) and during two Executive Board informal seminars. It was noted that the development of the Borrowed Resource Access Mechanism (BRAM) was a key element of IFAD's financial architecture reform.
36. The Committee benefitted also from the intervention of the Chair of the PBAS Working Group. Management highlighted that the paper presented on the BRAM mechanism is focused on principles and considers the following criteria:
- Country selectivity and eligibility: Three criteria as per IFAD11 (strategic focus, absorptive capacity and ownership) and level of indebtedness for BRAM only;

- Supply of borrowed resources: Committed/secured borrowing and planned borrowing, as defined in the resources available for commitment methodology, will be considered for financing;
  - Risk-based country limits: Such indicative risk-based country limits will be estimated as the prudent exposure to be maintained for each country in relation to its capital consumption;
  - Differentiated financing conditions: The principles contained in the graduation pillars will be respected; and
  - Demand-based access, in line with IFAD's mandate, government priorities and principles of development effectiveness.
37. In addition, Management noted that the update of financing conditions was the fourth of the five pillars of the BRAM. Management also highlighted that the proposed financing conditions were based on the overarching principles of differentiating financing conditions according to countries' economic trajectories, ensuring that low-income countries had the highest levels of concessionality. It was also noted that the current pricing structure used by IFAD would continue into IFAD12 on the condition that this ensured IFAD's financial sustainability. The changes would be implemented from IFAD12 onwards without retroactive effect.
38. Committee members requested some details on setting of risk ceilings/limits and on access prioritization. Members highlighted the need for consultation with countries and adequate reporting, and the importance of ensuring that the rates applied to BRAM financing exceed the average cost of borrowing. The principle of universality was stressed as well as the desirability of ensuring adequate supply of funds. Details were sought on studies to estimate demand while it was also pointed out the need for mechanisms in cases where there would be an imbalance between supply and demand.
39. While it was asked whether pricing could be used as a tool to incentivize challenging projects with high developmental impact, some Committee members asked why the initial proposal of introducing fees had been removed from this version of the document, noting that this was a common and expected practice and would ensure that IFAD covered the related costs of borrowing and hence ensure the financial sustainability of those elements. Management noted its wish for more-in-depth discussions with members before introducing fees.
40. Management provided details about risk ceilings and measures applied to the IFAD portfolio also to ensure financial sustainability. Management clarified the process that would determine the sequencing to access such funds and stated that yearly reporting would include details on BRAM resources.
41. The documents were considered as reviewed and would be submitted to the forthcoming Executive Board session for approval and for the endorsement of the related legal changes to be approved by the Governing Council in February 2022.
- Update on asset and liability management (AC 2021/160/R.9) – for review**
42. Management provided an update on the Asset and Liability Management Framework, noting the progress made since the last enhancement of the framework was approved by the Executive Board in December 2019, such as the collaboration between the Treasury Services Division and the Office of Enterprise Risk Management (RMO) through the recently signed internal service-level agreement, additional resources and the work done to map financial data.
43. Upon a question, Committee members were reassured on the adequate flexibility of the internal service-level agreement. The document was considered as reviewed.

**Enterprise risk management – for information**

44. Management presented an update on recent developments in enterprise risk management (ERM), touching on the work done by RMO since the end of 2020. It was noted that institutional risk maturity had been revisited and assessed as the basis for the effective operationalization of several areas of risk oversight and risk management. It was also noted that RMO had defined priorities and proceeded in acquiring resources, taking into due consideration existing tools.
45. Management provided details about risk governance noting that the establishment of risk committees would allow, among other things, to embed risk awareness more effectively within IFAD. Such committees would be the oversight focal point for the timely review of risks and for their monitoring. It was noted that there would be three technical committees reporting to the ERM Committee. Management also provided details on the progress being made in establishing an improved version of the corporate risk dashboard. Information was also provided on the importance of maintaining the credit ratings achieved and about the level of engagement with the rating agencies required to maintain them. IFAD was currently in the surveillance phase and in constant interaction with the agencies' analysts.
46. Committee members welcomed the update and noted the further steps to be taken amid the challenges deriving from the establishment of a risk culture.
47. The presentation was noted.

**Other business**

48. No additional items were put forward as other business.