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Report of the Chairperson on the 164th Meeting of the Audit Committee

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Executive Board — 135th Session
Rome, 25-27 April 2022

For: Information

Executive summary

1. In light of the COVID-19 pandemic, the 164th meeting of the Audit Committee was held remotely.
2. The Committee reviewed the following items, to be presented to the Executive Board at its 135th session:
 - Consolidated Financial Statements of IFAD as at 31 December 2021, including the Management assertion report and an independent external attestation on the effectiveness of internal controls over financial reporting and the High-level Review of IFAD's Financial Statements for 2021
 - Annual review of the activities of the Office of Audit and Oversight
 - Review of IFAD's Participation in the Heavily Indebted Poor Countries Initiative and potential ways forward
 - Medium-term Budget Outlook for 2023-2025
3. Under other business, Management provided a comprehensive update on the impact of the ongoing conflict in Ukraine on IFAD operations.

Report of the Chairperson on the 164th meeting of the Audit Committee

1. The Audit Committee wishes to draw the attention of the Executive Board to the matters examined at the 164th meeting of the Committee held on 24 March 2022. In light of the COVID-19 emergency, the meeting was held remotely by videoconferencing.

Agenda item 2 – Adoption of the agenda (AC 2022/164/R.1/Rev.1)

2. The agenda was adopted with the inclusion under other business of the following items:
 - Internal audit report on Burundi;
 - Internal audit report on Uzbekistan; and
 - Conflict in Ukraine: risks and impact for IFAD.

Agenda item 3 – Minutes of the 163rd meeting of the Audit Committee (AC 2022/164/R.2) – for approval

3. The minutes were approved with some edits, which were shared with members in advance of the meeting.

Agenda item 4 – IFAD financial statements

(a) Consolidated Financial Statements of IFAD as at 31 December 2021, including the Management assertion report and an independent external attestation on the effectiveness of internal controls over financial reporting (AC 2022/164/R.3 + Add.1 + Add.2 + Add.3) – for review

(b) High-level Review of the IFAD’s Financial Statements for 2021 (AC 2022/164/R.4) – for review

4. Management introduced this agenda item, noting the external auditor's unqualified audit opinion on the consolidated financial statements of IFAD as at 31 December 2021. For fiscal year 2021, Management confirmed the operational effectiveness of all key internal controls over financial reporting in the Management assertion report, with an independent attestation by the external auditor.
5. Management identified the key factors in IFAD’s financial position and reported results, emphasizing that despite the pandemic the overall financial situation was sound, with IFAD’s consolidated equity surpassing the US\$10 billion mark, and that long-term viability was being monitored closely. It was noted that at the end of December 2021, all financial ratios were within IFAD policy thresholds. Management expressed appreciation for the professionalism, hard work and contribution that Deloitte & Touche provided as their mandate comes to an end.
6. The external auditor provided details about audit work performed as part of the audit of the financial statements.
7. Committee members requested clarifications about information provided in the financial disclosures, including a comparison of the consolidated and IFAD-only financial statements, measures concerning non-performing loans and possible exposure deriving from certain conflict areas.
8. Management provided the requested information, noting that as a result of the conflict in Ukraine, IFAD had taken steps to comply with sanctions policies and procedures. It was also noted that the impact of the crisis would be captured in future macro-economic scenarios used as a basis to calculate the expected credit losses. Management also provided clarifications about debt servicing procedures and measures concerning expected credit losses and non-performing loans.

9. The consolidated financial statements and the high-level review of IFAD's financial statements for 2021 were considered reviewed and would be presented to the Executive Board at its 135th session for endorsement, prior to the Governing Council's formal approval in February 2023.

Agenda item 5 – Annual Report on the Activities of the Office of Audit and Oversight (AUO) during 2021 and review of the adequacy of the internal oversight mechanisms (AC 2022/164/R.5) – for review

10. AUO presented the report on internal audit and investigation activities in 2021. AUO highlighted that IFAD's substantial organizational, financial, workforce and business reforms had continued in 2021, putting pressure on both staff capacity and the control environment.
11. AUO's continued focus on auditing IFAD country programmes had brought to light some challenges in supervising programme implementation, especially project procurement, notwithstanding the significant strengthening of IFAD's project procurement oversight capacity in the last two years. It was noted that compliance with rules and procedures remained good throughout the organization while the revised delegation of authority framework was gradually being deployed, and the financial aspects of IFAD processes were positively assessed.
12. The AUO intake rate of allegations of misconduct and prohibited practices had levelled out in recent years but the number remained high, probably reflecting the inherent fraud and corruption risks in the organization's challenging operating environments. In parallel, AUO had stepped up risk mitigation efforts by sharing case status data through quarterly meetings with all key stakeholders, including the Programme Management Department, Financial Management Services Division and Financial Controller's Division.
13. In terms of staffing and resources, AUO's staff capacity had been reinforced in recent years with the addition of several new professional positions. However, AUO experienced high staff turnover in 2021. Notwithstanding the challenges, AUO delivered record outputs both in numbers and quality in 2021. Finally, AUO informed the Committee about a possible external review of its investigation function.
14. Committee members expressed their appreciation for the report and for the forthcoming external review. The Committee members raised the level of attention on the continuing challenges noted in relation to project procurement and the systemic implications and possible risk mitigation actions. AUO and Management provided further details on actions being taken and on the high priority Management is placing on this aspect. AUO further advised that when there was an IFAD presence in-country, with an IFAD Country Office or country director, audit findings were generally less severe. The Committee observed that there were no reported cases of harassment or sexual abuse in 2021 and AUO confirmed that this was the case.
15. The document was considered reviewed.

Agenda item 6 – IFAD's Proposed Private Placement Borrowing Transactions (AC 2022/164/R.6) – for review

16. The Committee considered IFAD's proposed private placement borrowing transactions in closed session and endorsed submission of the proposal to the Executive Board for approval.

Agenda item 7 – Medium-term Budget Outlook for 2023–2025 (AC 2022/164/INF.1) – for information

17. Management introduced the agenda item, noting IFAD's commitment to initiate a holistic multi-year budget planning exercise for the period 2023-2025 in order to provide greater predictability and transparency. Management noted that the medium-term budget would be driven by three main factors:

- Changes in the volume of programme delivery and the associated need to strengthen technical expertise and quality for deeper impact;
 - Increases in the cost of doing business with decentralization to more vulnerable countries; and
 - The broadening scope of IFAD's operations and activities.
18. Management indicated that three possible budget scenarios had been explored and that each scenario would require focused efforts for strategic prioritization. Committee members were also informed about potential future funding gaps.
 19. Committee members welcomed the presentation and the exercise as a kick start to more consultation going forward. They highlighted the importance of prioritizing, as well as possibly sharing costs with cofinancing partners and collaborating with other United Nations agencies and institutions.
 20. The presentation was noted.

Agenda item 8 – Review of IFAD's Participation in the Heavily Indebted Poor Countries (HIPC) Initiative and potential ways forward (AC 2022/164/R.8 + Corr.1) – for review

21. Management provided an update on IFAD's participation in the HIPC initiative since its inception, noting that since 1997 IFAD had been a committed participant in the process. The importance of alignment with the practices adopted by other international financial institutions was noted, as a way of preserving preferred creditor status, the non-performing loans ratio and the positive assessment by credit rating agencies. The Committee was informed that Sudan had reached the decision point in June 2021, just prior to the political turbulence, and was currently not in arrears with IFAD. The Committee was informed that Somalia had reached the decision point in March 2020. As Somalia had accumulated long outstanding arrears since the early 1990s, it would be a critical precondition to support the clearance of the remaining balance of US\$6 million to ensure a smooth debt relief process.
22. Committee members asked questions and made comments about the various options for debt relief. Some members requested additional details about measures taken by other institutions and the impact and timing of support. It was also observed that the financing mechanism for HIPC support should be discussed in a holistic manner, possibly within the IFAD13 Consultation.
23. Views varied among members regarding support for decision point for Sudan, with or without interim debt relief. This would require further discussion, which Management noted and would continue to consult further on.
24. Management highlighted the importance of aligning members' approaches among multilateral banks regarding both cases. Also, Management highlighted the possibility of considering approving the decision point without interim debt relief in the case of Sudan.
25. The document was considered reviewed and would be presented to the Executive Board together with the detailed document on HIPC decision point country cases.

Agenda item 9 – Draft provisional agenda of the 165th meeting of the Audit Committee – (AC 2022/164/R.9) – for review

26. The draft provisional agenda for the 165th meeting was reviewed, with no comments.

Agenda item 10 – Business continuity and effectiveness of working methods – Impact of COVID-19

27. Management provided an update on the business continuity and adaptation activities under way in response to the COVID-19 pandemic, highlighting progress made since the last update. It was noted that four offices remain in teleworking mode. The

teleworking pilot programme had been launched in October and 25 of the 801 staff members were working outside their duty station.

28. Some Committee members requested further details about lessons learned, country offices closed and the possibility of undertaking duty travel.
29. Management clarified that the offices still closed were those in Côte d'Ivoire, Haiti, Nigeria and Peru. Management informed the Committee that the alternative working arrangements had been launched in response to the first lockdown. It was also noted that country office audits carefully assess the delegation of authority and impact of decentralization.
30. The update was considered noted.

Agenda item 11 – Standard financial reports presented to the Executive Board – for review

(a) Report on IFAD's Investment Portfolio for 2021 (AC 2022/164/R.10)

(b) Financial Impact of Principal Due and Service Charges Forgone as a Result of the Implementation of the Debt Sustainability Framework (AC 2022/164/R.11)

(c) Report on the Status of Contributions to the Eleventh Replenishment of IFAD's Resources (AC 2022/164/R.12)

(d) Report on the Status of Contributions to the Twelfth Replenishment of IFAD's Resources (AC 2022/164/R.13)

(e) Status Report on Arrears in Principal, Interest and Service Charge Payments (AC 2022/164/R.14)

31. Management briefed the Committee on the investment portfolio report, which contained information as at end-December 2021. It was noted that performance up to December 2021 was slightly positive and that the size of the investment portfolio was comfortably above liquidity requirements. Management highlighted the risk of more market volatility, which it was addressing to ensure adherence to its objective of safeguarding liquidity and preservation of capital.
32. Management presented the status of the Twelfth Replenishment of IFAD's Resources (IFAD12), noting that pledges amounted to US\$1.22 billion, instruments of contribution amounted to US\$970 million and payments amounted to US\$338 million.
33. Some Committee members requested several clarifications about the IFAD12 target, the figures disclosed as Debt Sustainability Framework (DSF) compensation, the status of contributions to IFAD11 and the document Financial Impact of Principal Due and Service Charges Forgone as a Result of the Implementation of the Debt Sustainability Framework.
34. Management confirmed that IFAD12 pledges were expected to reach US\$1.3 billion, depending on one major donor and some other negotiations. It was clarified that the DSF compensation reflected in the status of IFAD11 contributions refers to principal compensation only and had been converted to United States dollars at the replenishment exchange rate.
35. The documents were considered noted and would be submitted to the Executive Board at its forthcoming session for information.

Agenda item 12 – Other business

(a) Update on the proposal to enter into a concessional partner loan agreement with the Republic of India to support the IFAD12 programme of loans and grants

36. Management informed the Committee that the proposal of a concessional partner loan from India in the amount of US\$20 million had been approved by the Executive Board by vote by correspondence dated 5 February.

37. The update was noted.

Agenda item 12(b) – Internal audit reports on the supervision of the country programmes in Uzbekistan and Burundi (IAR/22/01/Rev.1 and IAR/21/13/Rev.1 respectively) – for review

38. The Committee considered the internal audit reports on the supervision of the country programmes in Uzbekistan and Burundi in closed session. Members welcomed the updates from Management on actions being taken to address the findings of the report. Members also welcomed AUO's observation that while significant issues had been identified by the audits, Management took these issues very seriously and acted constructively in their follow-up, with procurement issues being treated as top priority.

Other business

39. Management provided a comprehensive update on the impact of the conflict in Ukraine on IFAD operations. The Committee was informed that senior Management had been monitoring the situation closely.
40. Management reported that although IFAD has no operations in the Russian Federation, Ukraine or Belarus, the crisis and the current situation on the ground had a major impact, since global prices of major commodities had risen significantly. The downside risk on the loan portfolio, especially for those countries that are heavily reliant on imported energy and food, was being monitored closely.
41. It was noted that several downgrades and a negative watch had been observed at other financial institutions, in particular the Asian Development Bank, the International Investment Bank, the Black Sea Trade and Development Bank and the New Development Bank. IFAD was in a different position with no direct exposure in the countries concerned. The Committee was informed that Management would monitor the evolution of the crisis to assess funding plans.
42. The Committee was informed that Management was exploring the possibility of establishing a new facility funded by supplementary funds (e.g. the financing facility for remittances, or the platform for agriculture risk management) or by additional core resources or additional concessional loans, or even by repurposing allocated resources.
43. Committee members welcomed the comprehensive update and looked forward to discussing it further within the Board.