Executive Board
140th Session
Rome, 11–12 December 2023

Internal Control Framework 2023

Document: EB 2023/140/R.11

Agenda: 3(c)(iii)(a)

Date: 6 November 2023

Distribution: Public

Original: English

FOR: APPROVAL

Useful references: Internal Control Framework EB 2019/127/R.39.

Action: The Executive Board is invited to approve the proposed changes to IFAD's Internal Control Framework.

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Contents

Executive summary

1. The present document contains the updates to IFAD's Internal Control Framework (ICF) (EB 2019/127/R.39) as provided for in section IX. An effective internal control system is rooted in robust governance and a commitment from the institution's leadership. The ICF mandates involvement by all IFAD personnel, and clearly defines their roles in upholding these controls. The ICF is interwoven with other key frameworks, thereby forming a comprehensive approach to risk and controls management to support transparency, oversight and accountability. The ICF is aligned with the principles of internal control set by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). It addresses risks that could impact IFAD's financial statements, and it mandates consistent monitoring of all significant business processes across IFAD. Leveraging the COSO model, IFAD's ICF is built upon five key components of internal control. The framework stresses the importance of roles and responsibilities, highlighting a three-line model: operational roles, specialized review, monitoring and challenge function, and assurance. Core standards such as the transactional authority model and segregation of duties underpin the functioning of the ICF. Implementation strategies include tools like the Controller's scorecard, training programmes and periodic reporting mechanisms. Exceptions to the ICF are managed with discretion to balance internal control standards with business efficiency. The monitoring of implementation of the ICF, including periodic updates, is managed by the Financial Controller's Division (FCD), with regular reporting to the Operational Risk and Compliance Committee (ORCC). Any relevant key risk indicators are included in the Corporate Risk Dashboard. The ICF is open to review by the Audit Committee on an ad hoc basis and approval by the Executive Board, as required.

2. The purpose of this update is to reduce duplication in areas now covered by the Enterprise Risk Management Policy and guidance; to focus on efficient and effective implementation of the ICF; and to streamline the document, removing analysis and references that are dated.

3. The proposed additions to the ICF are underlined and deletions are shown in strikethrough.

Internal Control Framework 2023

I. Introduction

1. An effective internal control system is founded on good governance and begins with a "tone at the top" that is consistent with the accountability framework. Under the Agreement Establishing the International Fund for Agricultural Development (IFAD) and regulation X of the Financial Regulations of IFAD, ultimate responsibility for establishing and maintaining appropriate internal financial controls rests with the President. In discharging this responsibility, the President is accountable to the governing bodies; and relies on delegation to and support from the Vice-President, Associate Vice-Presidents, Directors, internal governance mechanisms~~, other members of senior Management~~ and IFAD personnel.

2. A well-implemented internal control system involves the participation of all IFAD personnel – all of whom must understand their responsibilities. In fostering an effective control environment within the Fund, all personnel should proactively support and contribute to ~~operational risk~~ identification, assessment and – through the implementation of appropriate controls – mitigation. The Internal Control Framework (ICF) clarifies responsibilities for internal controls at IFAD.

3. The Enterprise Risk Management Framework (ERMF), IFAD Accountability Framework, Internal Control Framework (ICF) and Delegation of Authority (DoA) Framework are interrelated and work together as an integrated risk-based operational system of accountability, allowing for a holistic view of risk and control within the Fund. The Accountability Framework takes a functional view and sets out the core principles for ensuring transparency and accountability throughout the Fund, while the ICF sets out the optimal enabling standards and operationalizes IFAD's oversight and control models including DoA, as well as supporting good governance. The DoA Framework operationalizes accountability in a manner consistent with IFAD's control systems. The ERMF supports the identification, the assessment and the monitoring of risks and allows for a risk-informed decision-making. Together, these four elements comprise the foundation of IFAD's integrated accountability and control functions.

~~4. The ICF is essential for effective implementation of the ERMF at IFAD. The ERMF establishes risk policy, governance, appetite and tolerance in order to monitor, report and establish risk culture within the organization. ERMF principles are applied from strategy through execution while relying on internal controls at critical junctures. The ICF seeks to establish a foundation for implementing IFAD's internal controls with an approach derived from the ERMF that is consistent with the principles of the accountability framework and implemented through the Fund's governance structure by means of DoA.~~

Figure 1
Four elements of the foundation of IFAD's integrated accountability and control functions

Integrated approach enables risk-based/results-driven decision-making for optimal performance.

Enterprise Risk Management Framework

Risk-based approach to ~~manage IFAD and achieve results~~ determine appropriate balance between risk-taking and achieving IFAD's strategic objectives.

Internal Control Framework

Optimal control standards and effective ~~monitoring~~ assessment and reporting

IFAD Accountability Framework

Core principles for accountability and transparency

Delegation of Authority Framework

Decision-making authority structure

~~5. In addition to this framework, an ICF Implementation Guidance document has been prepared for consideration. The ICF will also be~~

4. The ICF is supplemented by various procedural documents ~~to be developed~~ and guidance shared with IFAD personnel.

II. Objective and scope

5. The ICF is designed to establish institutional standards and accountability for operating the internal control system. ~~by specifying: objectives and benefits; components of internal control, including the relevant policies, procedures, tools and responsible units; and the responsibilities of managers and personnel for the development, implementation, monitoring and improvement of policies and tools. The objective is to integrate several control mechanisms into one coherent and comprehensive framework. The ICF operational procedures will provide IFAD personnel with the required information and tools to implement the various requirements outlined herein.~~

~~III Definition of internal control at IFAD~~

6. IFAD's definition of internal control is aligned with that of the Committee of Sponsoring Organizations of the Treadway Commission (COSO),[1] as follows:

> *A process effected by IFAD's governing bodies, Management and other personnel that is designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting and compliance.*

~~IV. SCOPE~~

7. In order to protect IFAD's unqualified (clean) audit opinion, the ICF covers financial, operational, compliance and reputational risks to ensure an optimal standard of controls, all of which may have a significant impact on the Fund's consolidated financial statements. This approach requires review and ~~monitoring~~

[1] ~~COSO, *Internal Control – Integrated Framework* (2013).~~ COSO - Internal Control Integrated Framework, May 2013.

assessment of all significant business processes and the ~~operational~~ control risk related to these processes at the country and headquarters levels in order to ~~assess~~ identify key risks and ~~related~~ the areas where controls need strengthening. Existing processes related to operations such as the Social, Environmental and Climate Assessment Procedures (SECAP) and the IFAD Policy on Preventing and Responding to Sexual Harassment, Sexual Exploitation and Abuse will continue to be monitored through existing mechanisms.

~~V. Benefits and underlying principles~~

III. Benefits

8. The ICF establishes principles for the development, implementation and monitoring of controls with the following benefits to the Fund and its Member States:

   (i) ~~Provide for effective, efficient~~ Creates a mechanism to assess and ~~leaner~~ adjust on a regular and systematic basis to ensure optimal controls~~ that address operational and other non-financial risks~~, including ~~by minimizing risks associated with~~ management of decentralization ~~and the evolution of IFAD's business model~~ risk;

   ~~(ii) Maintain and improve the completeness, accuracy, reliability, appropriateness and timeliness of financial and non-financial information;~~

   (ii) Dedicates resources to support implementation of an effective ICF across IFAD;

   (iii) Provides ~~necessary~~assurance to the signatories of IFAD's consolidated financial statements ~~and~~ on the effectiveness of internal controls globally supporting an unqualified (clean) audit opinion;

   (iv) ~~Ensure the~~ Supports IFAD's observance of legal, statutory and related obligations~~applicable to IFAD, including ethical standards and rules~~;

   (v) Aims to reduce risk of fraud and error, including

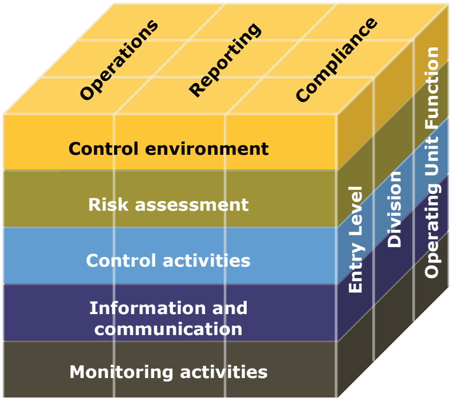
   ~~(v)~~ ~~Reduce~~ losses and waste of assets and resources;~~, whether through misdirected effort, avoidable errors, mismanagement, abuse or fraud;~~ and

   (vi) Sustains and increases confidence among Member States and other stakeholders in the reliability, resilience and efficiency of IFAD's internal control and management systems.

IV. Application of the five components of internal control

9. IFAD's ICF is based on the COSO model of internal control. This model sets out the five interrelated components of internal control ~~control environment; risk assessment; control activities; information and communication; and monitoring activities. All are required for an integrated and effective internal control system. The five components and supporting principles are~~ set forth below.

Figure 2
The COSO cube



* See COSO, *Internal Control – Integrated Framework* (2013).

10. **The control environment** ~~includes~~ is the ~~standards, processes~~ foundational tone and ~~structures that~~ structure set by an organization, encompassing its ethical values, management style, and the direction provided ~~the basis for carrying out~~ by its governing body, influencing the overall internal control ~~at IFAD. It also comprises the authority with which senior Management oversees the performance of control activities; recruits, develops and retains competent personnel; and holds individuals accountable for their actions~~ system.

11. **Risk assessment** is a dynamic and iterative process for identifying, assessing, prioritizing and managing key risks to support the achievement of IFAD's objectives. Risk to the achievement of these objectives from across the entity are considered relative to established risk tolerance. Thus, risk assessment forms the basis for determining how risk will be managed.

12. **Control activities** are the actions ~~carried out~~ established by policies and procedures to ensure ~~that the Executive Board's directions on risk management are carried out, including its stated risk appetite~~ risks are mitigated and Management's objectives are achieved. They can be preventive or detective in nature and can include both manual and automated tasks like authorizations, verifications and reconciliations.

13. **Information and communication** ~~from internal and external sources enables IFAD to assess how well the different elements of its control~~ provide a system ~~are~~ to ensure timely and effective sharing of pertinent information, both internally and externally, supporting ~~the achievement of its objectives~~ staff in fulfilling their roles within the internal control process.

14. **Monitoring activities** ~~keeps track~~ are practices developed and used by Management to focus simultaneously on analysing and reporting on the success of ~~the operation~~ these procedures in terms of ~~internal~~ controls ~~through ongoing and one-time evaluations to confirm that required controls are present, functioning and successfully managing risks to~~ and the achievement of ~~IFAD's~~ objectives.

~~Table 1~~
~~**Internal control components and applicability at IFAD**~~

~~*Component*~~	~~*Examples of applicability at IFAD*~~
~~Control environment~~	~~Procedures, standards and reporting~~
~~Risk assessment~~	~~Will be implemented with the ERMF (e.g. new risk assessments for business processes, existing risk assessments for fiduciary risk at the project level)~~
~~Control activities~~	~~Will be implemented within the Risk Appetite Framework and ICF Implementation Guidance~~
~~Information and communication~~	~~Will be implemented through reporting, risk and controls awareness-raising, and a communication plan~~
~~Monitoring activities~~	~~Will be implemented with monitoring tools and building blocks (see figure 4)~~

15. The COSO framework was initially applied at IFAD in 2012 through the development of IFAD's internal controls over financial reporting (ICFR) process. It includes the mapping of the significant business processes impacting financial reporting – highlighting the risks and related controls associated with each process – and ~~is being~~ extended through the ICF to all business processes across IFAD.

~~VII Roles and responsibilities for internal control~~

V. Roles and responsibilities for internal control <u>mechanisms</u>

16. The creation of an effective internal control function is ~~grounded in~~ <u>adapted from</u> the Institute of Internal Auditors (IIA) three lines of defence model[2] ~~(see figure 3), which is consistent with the model recommended by the Basel Committee on Banking Supervision and Bank for International Settlements[3] and leading industry practice.~~<u>as detailed below, and pertains to internal control mechanisms:</u>

- **The first line of defence <u>roles:</u>** ~~comprises front-line business and support units, which take on risks and are expected to manage and mitigate them. They are also expected to apply controls consistent with the ERMF and IFAD's risk appetite~~<u>direct actions, own and manage risks, and allocate resources to achieve organizational objectives; engage in continuous communication with governing bodies, reporting on outcomes and risks related to the organization's goals; set up and oversee structures and processes for operations, risk management and internal control; and ensure adherence to legal, statutory and ethical standards.</u>

- **The second line of defence <u>roles:</u>** ~~includes, among others, the safeguards and~~ <u>offer specialized support in</u> risk <u>and internal controls</u> management ~~functions performed by~~<u>aiding in</u> the ~~Accounting~~ <u>development</u> and ~~Controller's Division (ACD) Controllership Unit~~ <u>enhancement of risk</u> and ~~financial and other~~ <u>control practices at various levels. Second line of defence roles also evaluate and report on the adequacy of</u> risk management ~~units, which: assess~~ <u>measures, ensuring compliance with internal control, information and technology security, legal, ethical and other standards. This includes</u> the ~~risks being assumed, the controls being implemented (independent from first line of defence functions) and enable the monitoring of~~ <u>provision of digital solutions to enhance internal</u> controls <u>and minimize manual steps where possible.</u>

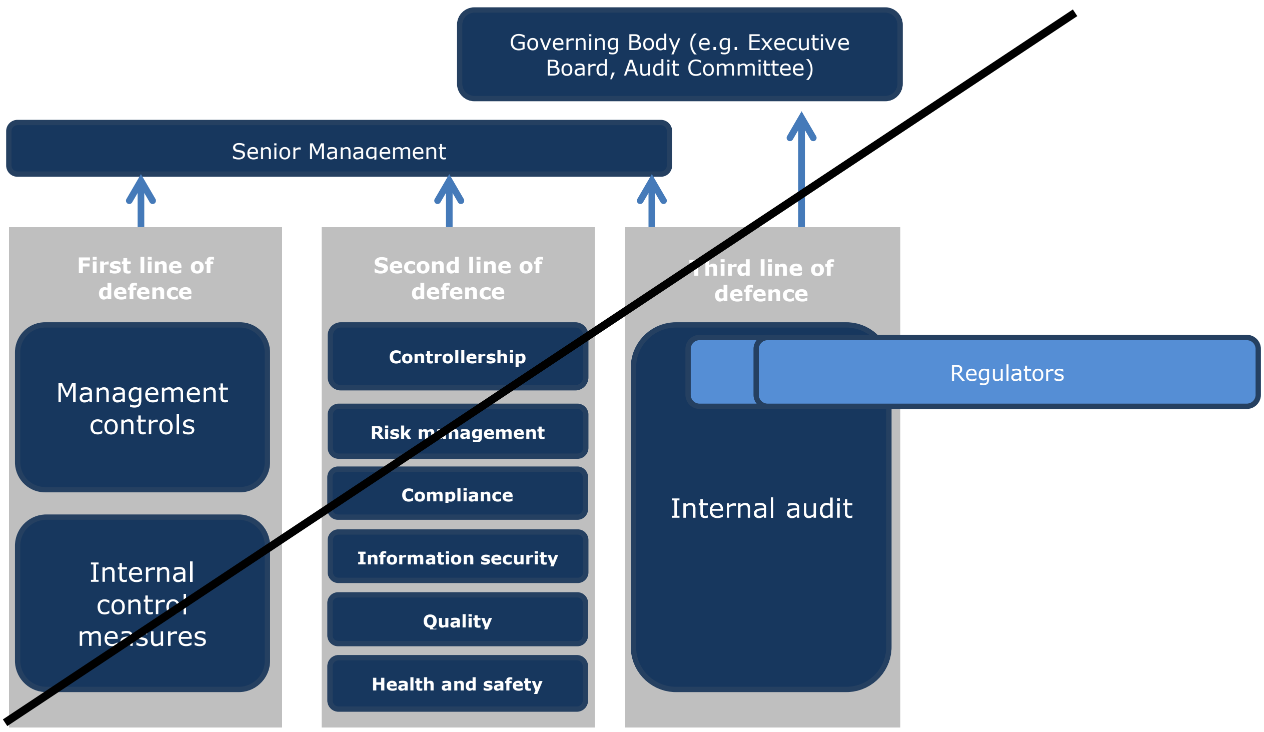
- **The third line of defence <u>roles:</u>** ~~comprises functions such as~~ <u>include</u> internal audit, which provides ~~ex post audit assessments of compliance, examines the adequacy of controls to mitigate risks, and identifies cases of non-compliance through ex-post reviews. IFAD's applicationof the three lines~~

~~[2] IIA, *The Three Lines Of Defense In Effective Risk Management And Control*, IIA Position Paper (2013).~~
~~[3] See Bank for International Settlements, Occasional Paper No 11, The "Four Lines of Defence Model" for Financial Institutions (2015).~~

~~of defence model is presented in figure 3 below.~~ unbiased assurance to both management and the governing body on governance and on the effectiveness of risk and controls management, reporting any conflicts of interest and implementing necessary safeguards. Third line of defence roles also include external assurance providers, which provide additional assurances in order to meet statutory requirements for stakeholder protection and to fulfil management and governing body requests for added internal assurance.

17. Close interaction and regular consultations between the first, second and third line of defence roles is required for effective implementation.

~~Figure 3~~
~~**Institute of Internal Auditors three lines of defence model**~~



~~**First line of defence functions (excluding those presented in the second and third lines of defence)**~~

18. ~~First line business units are the ultimate risk owners within the organization. They are accountable for operationalizing internal controls as prescribed in IFAD's regulations, rules, policies and procedures. IFAD personnel within these units must ensure that proper controls are embedded within their processes. They are responsible for identifying opportunities to improve the effectiveness and efficiency of controls, and for responding promptly to any identified gaps or weaknesses in these controls – either by remedying them or escalating them through established reporting mechanisms. IFAD personnel should escalate any control deficiency, non-compliance, risk or other operational problem that threatens the achievement of IFAD's objectives to their respective Senior Management member and engage second line of defence functions as needed.~~

~~**Second line of defence functions**~~[4]

19. ~~As presented in figure 3, there exist multiple second lines of defence functions. The paragraphs below outline the key functions related to control and risk.~~

[4] ~~Aspects of second line of defence functions may be carried out within other units such as the Operational Policy and Results Division.~~

20. ~~The ACD Controllership Unit is a second line of defence function aimed at implementing and ensuring compliance with IFAD's ICF. It implements and conducts assessments, and monitors and reports on IFAD's internal controls, highlighting weaknesses that would expose IFAD to risks. It also provides advice, expertise and tools for risk mitigation both at headquarters and in decentralized offices to ensure that adequate internal controls and reporting processes are in place and functioning optimally. In addition, the unit promotes a culture of internal control awareness: on the one hand, the unit aims to strike a balance between business objectives and control measures in order to protect IFAD against risks and support its unqualified (clean) audit opinion and, on the other, promote efficiency in its operations.~~

21. ~~The Risk Management Unit, within the Financial Operations Department (FOD), is a second line of defence for financial risk management at IFAD.~~

22. ~~The Ethics Office promotes compliance with the Fund's rules, policies and procedures, including the IFAD Code of Conduct, and fosters a culture of ethical behaviour, transparency and accountability. The Ethics Office also manages the Fund's financial disclosure and mediation programmes.~~

23. ~~A second line of defence lies within the Office of the General Counsel, which aims to protect the Fund from legal risks and provide advice on the Fund's broader legal interests, including in relation to operations, policy development and dispute resolution. It provides second line legal advice and support to the President and governing bodies, ensuring that IFAD's activities are carried out in accordance with the Agreement Establishing IFAD and other rules and regulations.~~

24. ~~There is a second line of defence function related to information security within the Information and Communications Technology Division (ICT), which provides a sustainable and secure digital environment; mitigates cyber security risks; and facilitates, together with business owners, a culture change to understand the value of information assets.~~

~~Third line of defence functions~~

25. ~~The responsibility for auditing and evaluating controls, and for providing Management, governing bodies and other stakeholders with assurance of these controls, is delegated to the Office of Audit and Oversight. As a third line of defence, this office provides independent, objective assurance to the Audit Committee and Executive Board on the effectiveness of IFAD's internal controls in order to ensure that critical financial and operational risks are being managed appropriately, and that the internal control system is operating effectively.~~

~~Cooperation between the three lines~~

26. ~~The first and second lines will have ongoing interactions and consultations with each other in particular for loss/incident reporting processes as well as over monitoring and reporting tools implementation. The second line assists the first line to establish and enhance controls within their business processes and provide monitoring support related to relevant frameworks and their respective implementation plans. Additionally, support and oversight are provided through the risk assessments.~~

27. ~~The multiple second line units should interact with each other, to ensure an integrated and harmonized approach to risk and control within IFAD.~~

28. ~~The second line should work closely with the third line, relying on reports by the third line to inform of risks and weaknesses identified, as well as provide the third line with the results of monitoring to enhance IFAD's overall controls.~~

29. ~~There should be close interaction and consultations between first, second and third line to ensure alignment regarding common areas of control weakness and~~

~~continuous communication to exchange results and outcomes following assessments.~~

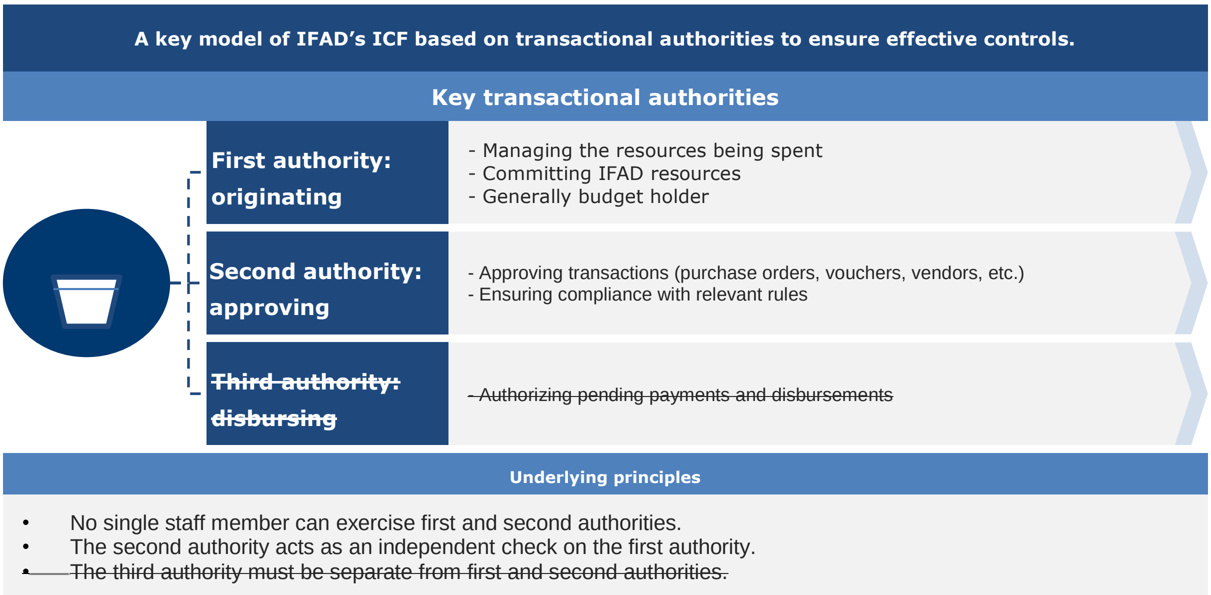
VI. Core control standards

30. An effective internal control system is founded on a set of control standards. ~~In order to establish optimal internal controls, an organization must identify and implement appropriate control standards that are based on its operations and overall exposure to risk. In light of the evolving business model and decentralization, the following section outlines the two core control standards that become increasingly important to IFAD in the decentralized environment. Additional control standards are outlined in the ICF Implementation Guidance document.~~ The two core control standards are transactional authority model and the segregation of duties.

31. The transactional authority model is a mechanism that mitigates the risk of inappropriate transactions. It also serves as a deterrent for fraud and enforces segregation of duties. The segregation of duties is the concept of having more than one person required to complete a task.

32. Each transaction or process requires at least ~~three~~ two levels of transactional authority from establishment to completion ~~These authorities are exercised for all IFAD loans and grant disbursements, procurement, commitments, payments received and expenses (payroll, administrative, travel and consultants, etc.). They are an important element of an effective internal control system.~~ which reduces the risk of fraud and or error. IFAD being a smaller organization, largely automates the disbursement authority over the years with the move to streamlined processing and straight-through-processing where in many cases the second transaction authority also effects disbursements or where no further substantive controls are undertaken at the point of disbursement given the ex ante checks and balances implemented. Control testing findings conducted by Controllership might be reported to the Office of Enterprise Risk Management and Office of Audit and Oversight as deemed necessary.

~~Figure 4~~
Figure 3
Key transactional authority model



33. **First transactional authority – originating:** has the primary responsibility for managing the resources being spent, ensuring the proper commitment of IFAD's resources and managing the underlying task or objectives.

34. **Second transactional authority – approving:** verifies and approves transactions (e.g. loan and grant disbursements, purchase orders, vendor registration, payroll), ensuring that the related requests are compliant with relevant policies, procedures and guidance.

~~35. **Third transactional authority – disbursing:** authorizes the execution of payments and disbursements.~~

~~35. No single person can exercise more than one transactional authority over any one transaction, since each transactional authority acts as an independent check on the previous one. Given the nature of these controls, they must be performed by IFAD staff members. Multiple approvals may be required within each stage of the transactional authority model.~~

~~**Segregation of duties**~~

35. Segregation of duties occurs when two or more individuals are required to complete a transaction to reduce the likelihood of error or fraud. An additional element of segregation of duties is, normally and where practical, separation of duties for the following areas: custody of assets, authorization, recording and reconciliation of the transactions. ~~The likelihood of error or fraud diminishes significantly when two or more individuals are involved in processing the transaction. The segregation of duties ensures an appropriate level of checks and balances by allowing one person to verify that transactions initiated by another are properly authorized, recorded and settled. When establishing standards for the segregation of duties, Management should assign responsibilities so that a single person cannot effect an entire transaction from inception to completion. For example, personnel that originate transactions should not approve the transaction.~~

36. Automated controls that act in a similar way to manual segregation-of-duty controls can be written into software programmes~~; for example in PeopleSoft. When properly designed, automated controls can be superior to manual procedures. Unique system profiles and access and rights controls within PeopleSoft (or other software) constitute fundamental system controls. IFAD's PeopleSoft and other software (e.g. FlexCube) reinforce the control of segregation of duties, ensuring that one user profile cannot perform multiple approvals on a given transactions~~.

37. ~~More efficient and effective internal control automation can be achieved by adopting robotic process automation, i.e. using bots to perform controls. This further enhances the control of segregation of duties, since the bot profile is programmed to perform as one user only and there is no risk of multiple approvals.~~

~~IX. Providing oversight and monitoring internal controls~~

~~39. Figure 5 outlines the overall oversight and monitoring tools. The ACD Controllership Unit aims to institute and/or strengthen the following mechanisms for assessing the effectiveness of internal control:~~

~~(i) **Control self-assessment process**. All managers and other personnel will complete a control self-assessment exercise, as outlined in the IFAD Control Self-Assessment Manual. This manual will provide managers and other personnel with details needed to perform control self-assessments, including tools and related references. The process will include periodic self-assessments performed by the originating divisions/units and reviewed by the ACD Controllership Unit, which will help to identify control gaps and key risk indicators.~~

~~(ii) **Incident-reporting process**. All personnel will be required to report operational risk-related loss incidents and "near misses" following a defined reporting process.~~

VII. Implementation of the ICF

38. The following will be undertaken to implement the ICF:

(i) **Controller's scorecard** as an outcome to Controllership support missions. A reporting tool as part of the conclusion report of each FCD review highlighting areas of strength and or weakness in controls and recommended action and support. This is the outcome of the control testing, discussions with key staff, managers/directors/leadership, review of internal and external data and reports, the controllership questionnaire, assessment of delegation of authority, and physical or desk review missions; ~~A monitoring tool that will be used by the ACD Controllership Unit to measure current and potential losses, and key risk indicators, and highlight the financial health of the Fund's operational risk and control environment.~~

(ii) **Internal control and delegation of authority certification.** A signed document that attests to the required standards of internal control in a department/division/office/unit. There is also a separate DoA annual certification by delegees and subdelegees attesting to implementing DoA as required;

(iii) **Training and awareness.** Regularly scheduled training and awareness programmes to embed control culture at IFAD headquarters and in IFAD offices globally.

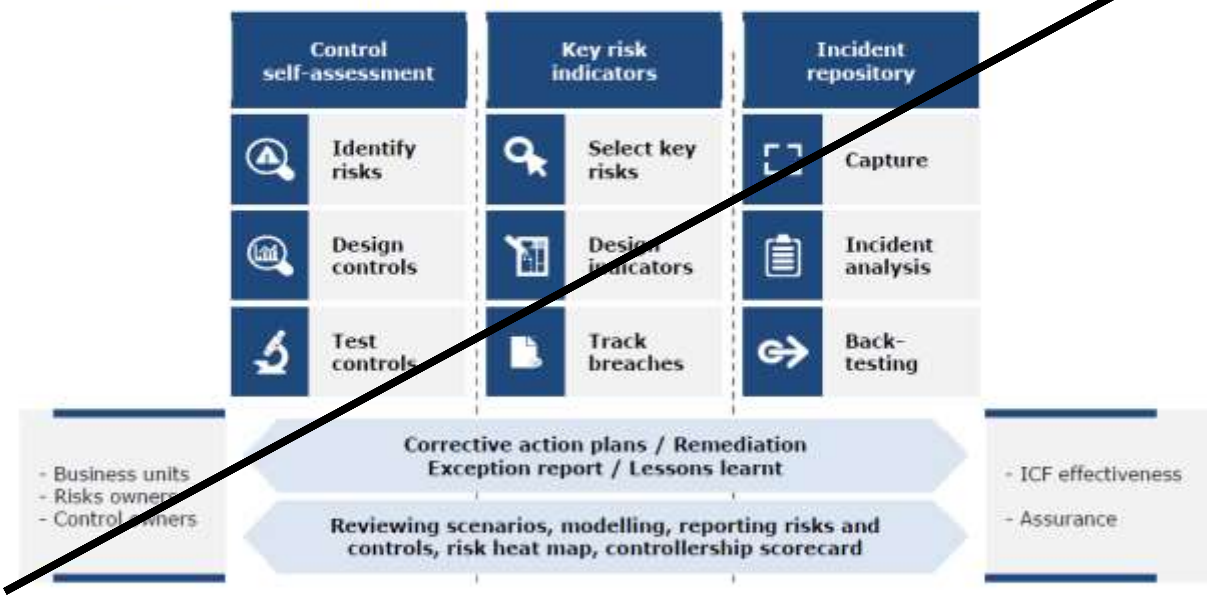
(iv) **Reporting to Operational Risk and Compliance Committee (ORCC).** Regular reporting on weaknesses in internal controls, outcomes of Controllership review and support missions, delegation of authority and digital tools will be undertaken;

(v) **Indicator(s) on the IFAD Corporate Risk Dashboard**. IFAD has established a corporate risk dashboard that is reviewed by governing bodies at regular intervals. Relevant indicator(s) relating to the ICF will be established to facilitate reporting on internal controls to governing bodies; ~~The dashboard has been developed to monitor key risks, facilitate the flow of information and enable decision-making on risk management issues. It can also be used to report on the measurement and management of risks to the Audit Committee and Executive Board.~~

(vi) **Management assertion report on the effectiveness of internal controls over financial reporting (ICFR)**. The President; the Associate Vice-President, Chief Financial Officer and Chief Controller, Financial Operations Department; and the Director and Controller, ~~ACD~~ FCD currently provide an annual assertion of the effectiveness of IFAD's internal controls over financial reporting;

(vii) **External auditors** currently provide an attestation of the Fund's internal controls over financial reporting and accounting procedures.

Figure 5
Oversight and monitoring of internal controls



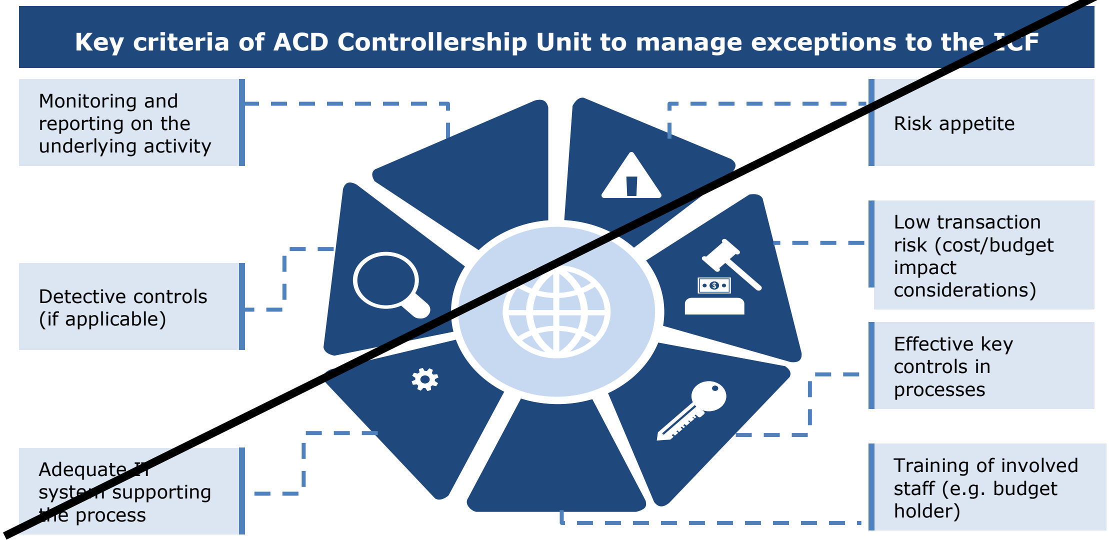
VIII. Exceptions ~~to the ICF standards~~

39. The ICF presents the **optimal standards for internal controls** such as segregation of duties and levels of transactional authority. Where exceptions are required, FCD will use criteria developed and shared internally (as well as to ORCC where required), in order to uphold the high standards of internal control taking into consideration business efficiency. FCD will propose compensating controls, preferably through automation, and an action plan in consultation with the originating unit. With the right level of automation, the originating unit will be able to introduce compensating controls that do not require an additional effort.

~~40. Some smaller offices may require exceptions to the ICF standards, for example in IFAD's decentralized model. In such cases, exceptions are to be requested from the ACD Controllership Unit, which will provide direction on compensating controls and other risk mitigation measures in order to ensure that IFAD remains compliant and within its risk appetite.~~

~~41. The ACD Controllership Unit will assess exception requests against the key criteria presented in figure 6 and detailed in paragraphs 43 and 44. Following the assessment, if an exemption can be granted, the ACD Controllership Unit will propose compensating controls or an action plan in consultation with the originating unit and may increase monitoring activities.~~

~~Figure 6~~
~~**Key criteria for exceptions**~~



~~42. When exemptions are requested, the ACD Controllership Unit will conduct a risk assessment against the seven key criteria noted in figure 6 to ensure that the acceptable level of residual risk is maintained.~~

~~43. The following criteria must be met for the exemption to be considered.~~

~~(a) **Risk appetite**: Upon review of the proposed exemption to an internal control standard, the ACD Controllership Unit will assess the residual risk that would result if an exemption is granted. In order to meet this criterion, the residual risk must be below IFAD's risk appetite limits.~~

~~(b) **Low transaction risk**: Residual risk as assessed in subparagraph 43.a must be below a set materiality threshold to minimize its potential impact on the consolidated financial statements.~~

~~(c) **Effective key controls in processes**: Existing key controls must be embedded within the process being considered for exemption. In order to meet this criterion, the process must have sufficient controls (detective or preventive) in place.~~

~~(d) **Level of skills/training of involved staff**: Affected staff must have adequate training on the process being considered, including training in assessing relevant risks and implementing adequate controls, which will help reduce risks associated with a potential exemption.~~

~~44. The following additional elements support the approval of the exemption.~~

~~(a) **Monitoring and reporting**: The activities under consideration are already subject to periodic reporting to ensure ongoing monitoring of those activities.~~

~~(b) **Detective controls**: Detective controls are to be implemented prior to approval of the exemption in order to mitigate the risks identified in the assessment.~~

(c) ~~**Adequate IT system supporting the process**: Automation embedded in the process reduces the likelihood of operational risk, providing greater assurance of acceptability.~~

~~XI.Application, approval and updates~~

IX.Governance, approval and updates

44. The ICF will be implemented in IFAD supported by the Financial Controller's Division (as custodian of the ICF. The custodian will issue relevant procedures and guidance, and carry out monitoring and reporting to fully and effectively implement the framework. Reporting on implementation of the ICF, including control weaknesses and matters relating to delegation of authority, will be undertaken on a regular basis by the custodian to the Operational Risk and Compliance Committee (ORCC), which may escalate issues to the ERMC as deemed necessary. The ICF and any updates to it are to be presented to the Audit Committee for review and the Executive Board for approval on an ad hoc basis as deemed necessary. ~~within IFAD effectively and efficiently. The ICF will be presented to the Audit Committee for review and Executive Board for approval. To ensure that the ICF remains relevant, it will be updated by the ACD Controllership Unit every three years and ad hoc reviews may be effected as deemed necessary. In addition, the ICF will be updated to ensure alignment with the revised Enterprise Risk Management Policy, which includes internal governance, accountability, risk taxonomy definitions and risk appetite. All interim revisions and amendments to the ICF outside of the three-year cycle will be approved by the President and submitted for information to the Audit Committee and Executive Board~~.

~~Glossary~~

~~Accountability~~
~~The obligation of an organization and its staff to be responsible for delivering specific results that have been determined through a clear and transparent assignment of responsibility, subject to the availability of resources and in line with applicable polices, rules and procedures. Accountability includes: achieving objectives and results in response to mandates; fair and accurate reporting on performance results; stewardship of funds; and all aspects of performance.~~

~~Compliance Risk~~
~~Monetary cost/loss (sanction), material loss or loss to reputation to which IFAD may be exposed, arising from a failure to comply with internal policies, applicable rules, regulations, laws and international standards of good practice.~~

~~Control self-assessment~~
~~The control self-assessment process is an integral element of IFAD's operational risk framework, which integrates its risk identification and management efforts. Its aim is to enhance Management's understanding, oversight and control of operational risks. It supports corporate objectives by measuring operational risk and aligning capital assessments.~~

~~Inherent risk~~
~~Inherent risk is the risk prior to controls being put in place (impact multiplied by probability factor). It is the amount of risk in the absence of any direct or focused actions by Management to mitigate its impact and likelihood.~~

~~Key controls~~
~~Key controls are interventions taken to reduce a risk to an acceptable level. Reducing risk means reducing the probability and severity of an adverse event. When well designed and operating effectively, key controls mitigate inherent risk.~~

~~Key risks~~
~~Key or important risks can be defined as internal or external events that have the potential to impact achievement of the Fund's overall objectives or those of an individual business unit.~~

~~Key risk indicators~~
~~These indicators comprise qualitative, quantitative or judgmental measures set by Management for the most important areas of risk facing the Fund. They recognize improvements or deteriorations in operational risk levels and exposures, and are monitored and assessed with the aid of escalation triggers. Assessed through control self-assessments (both first and second line), they are monitored by combining results across the Fund at both the headquarters and regional levels. They can be forward-looking indicators of shifts in risk trends.~~

~~Management~~
~~For the purposes of this framework, Management includes Senior Management, directors, heads of offices and hubs, and country directors.~~

~~Senior Management~~
~~For the purposes of this framework, senior Management includes the President, the Vice-President, the Associate Vice-Presidents, the Office of the President and the Chief of Staff.~~

~~Personnel~~
~~For the purposes of this framework, personnel includes all IFAD staff, interns, consultants and anyone else employed by IFAD.~~

~~Operational risk~~

~~Risk arising from inadequate or failed internal processes, people and systems, or from external events (e.g. fraud).~~

~~Operational risk source (or event)~~

~~The Basel Committee on Banking Supervision's categorization of events includes:~~

~~(i) Internal fraud – the misappropriation of assets, tax evasion, intentional mismarking of positions, bribery;~~

~~(ii) External fraud – theft of information, hacking damage, third-party theft, forgery;~~

~~(iii) Employment practices and workplace safety – discrimination, workers' compensation, employee health and safety;~~

~~(iv) Clients, products and business practices – market manipulation, antitrust, improper trade, product defects, fiduciary breaches, account churning;~~

~~(v) Damage to physical assets – disasters, terrorism, vandalism;~~

~~(vi) Business disruption and systems failures – utility disruptions, software failures, hardware failures; and~~

~~(vii) Execution, delivery and process management – data entry errors, accounting errors, failed mandatory reporting.~~

~~Operational risk impact~~

~~The impact of operational losses can be evidenced by financial losses, penalties, compensation to clients or third parties, and increased costs from corrective actions or write offs.~~

~~Reputational risk~~

~~Risk arising from a negative perception on the part of customers, counterparties, shareholders, investors or regulators that can adversely affect an institution's ability to maintain existing or establish new business relationships and continued access to sources of funding.~~

~~Residual risk~~

~~Residual risk is the assessed risk after controls are put in place (impact after detective controls multiplied by probability factor after preventive controls). It is the amount of risk that remains after taking into consideration the controls that have been established for its mitigation.~~

~~Risk scoring matrix~~

~~The risk scoring matrix is used to assess or calculate inherent risk. It is the superimposition of the impact axis on the probability axis. Numerical values (1-5) are applied to determine the severity of the impact on the achievement of objectives should the event occur, and the probability of its occurrence.~~