



**IFAD**  
**INTERNATIONAL FUND FOR AGRICULTURAL DEVELOPMENT**  
**Executive Board - Sixty-Fifth Session**  
Rome, 2-3 December 1998

**REPORT OF THE AUDIT COMMITTEE**

1. Following its Sixty-Fourth Meeting on 1 December 1998, the Audit Committee (the Committee) wishes to report the following matters to the Executive Board.

**Revised Terms of Reference and Rules of Procedure of the Audit Committee**

2. At its Sixty-First Session in September 1997, the Board decided to change the composition of the Audit Committee, thus necessitating a revision of the Committee's terms of reference and Rules of Procedure. The Committee thoroughly reviewed a draft document provided by the Secretariat clarifying the responsibilities and authority of the Audit Committee in relation to External and Internal Audits. The Committee draws the attention of the Executive Board to document EB 98/65/R.38 and, in particular, to the annex to that document containing the revised terms of reference and Rules of Procedure of the Committee, together with the original text. The Executive Board is invited to approve the revised terms of reference and Rules of Procedure of the Audit Committee.

**General Reserve - A Review of Adequacy**

3. The Committee began its review of the adequacy of the General Reserve with discussion on a proposal to increase the ceiling of the General Reserve from USD 100 million, approved by the Governing Council at its Fourth Session in December 1980, to USD 130 million. The Committee also discussed the transfer of USD 5 million to the General Reserve from the Accumulated Surplus of IFAD's Resources for 1999, which would bring the amount of the approved transfer to the General Reserve approved by the Executive Board to USD 100 million. As further discussion will be required, the Committee has included this item on the agenda of its April 1999 meeting. The Committee noted that any recommendation by the Executive Board to increase the General Reserve ceiling would require Governing Council approval. The Committee felt it would not be desirable to leave the matter in abeyance until the Governing Council meets during the first quarter of 2000, and accordingly recommended that the Governing Council, at its Twenty-Second Session in February 1999, delegate authority to the Executive Board to amend the ceiling of the General Reserve.

**Provision for Unfunded Liabilities**

4. The Audit Committee also discussed the issue of After-Service Medical Scheme costs, as communicated to the Executive Board in the context of the Programme of Work and Budget of IFAD



for 1999. A proposal to make annual transfers of USD 2.6 million from the Accumulated Surplus of IFAD's Resources in each of the five consecutive years commencing with 1999, so as to build up a provision of USD 13 million to fund the After-Service Medical Scheme actuarial deficit, was considered. The introduction of Common Accounting Standards within the UN system, as endorsed by the General Assembly, will require organizations to recognize the costs incurred but not-yet-paid-for post-retirement benefits on the basis of an actuarial valuation. For international financing institutions such as IFAD, International Accounting Standards (IAS) require that the cost of providing employee benefits should be recognized both as a liability and as an expense. Revised IAS 19 stipulates that an actuarial valuation should be used to make a reliable estimate of the amount of benefits that employees have earned in return for their service in the current and prior years.

5. The Food and Agriculture Organization of the United Nations (FAO) (whose financial statements are produced under the less stringent United Nations Common Accounting Standards) decided to amortize the unfunded actuarial deficit over a 30-year period. However, IFAD is obliged to comply with the requirements of the IAS. The latter, which takes effect for accounting periods beginning 1 January 1999, provides two alternatives to deal with the actuarial deficit. The first is to recognize the deficit immediately, that is, to make provision for the USD 13 million against the opening balances of the accumulated surplus. The second alternative is to treat the deficit as an expense on a straight-line basis over a five-year period from the date of adoption (paragraph 155 of revised IAS 19).

6. Given that immediate recognition of such liability would have an adverse impact on IFAD's resources available for commitment, the Audit Committee recommends to the Executive Board that the second alternative be adopted, that is, amortization on a straight-line basis over a five-year period starting in 1999. The deficit would be accordingly extinguished by five annual allocations of approximately USD 2.6 million from the accumulated surplus.

7. The Executive Board is invited to approve this action.

#### **Recommendation on the Remuneration of the External Auditor**

8. The Committee is required to make a recommendation each year on the remuneration of the External Auditor. Price Waterhouse has proposed an audit fee for 1998 of ITL 162 million, plus out-of-pocket expenses. This proposal represents a decrease of ITL 11 million over the actual audit fees of 1997, based upon two factors: (a) an increase of ITL 1 million in the fees for auditing the IFAD Supplementary Funds as a result of a greater number of trust funds; and (b) a decrease of ITL 12 million in audit fees for IFAD's Regular Resources. Costs in 1997 for additional work in the area of investments were billed separately, whereas, from the 1998 audit, this will become an ongoing element of the annual audit. The cost of living increases of approximately ITL 3 million have been offset through greater efficiency. At its April 1999 meeting, the Committee will consider ways of bringing together its consideration of the scope of the Audit and the establishing of the Auditor's fee for the work.

9. The Committee recommends that the Executive Board approve an audit fee for 1998 of ITL 162 million, plus out-of-pocket expenses.

#### **Annual Review of Internal Audit**

10. In making its first annual review of the Internal Audit system, the Audit Committee reaffirmed the importance of, and welcomed the increased attention that IFAD's management had given to, the internal audit function over the past year. The Committee:



- noted and welcomed a report by the Chief, Internal Audit, summarizing activities undertaken in 1998 and the planned programme for 1999;
- noted that the proposed 1999 programme assumed the allocation of additional resources as part of the 1999 Programme of Work and Budget;
- decided to reflect further at its first two meetings in 1999 on the most appropriate way of reviewing the output of the Internal Audit system (bearing in mind that all Internal Audit reports are provided to the External Auditor, who takes them into account in preparing his annual Memorandum on Internal Control); and
- decided that future annual reviews of the Internal Audit system would be undertaken by the Committee at its April meetings, starting in 1999.

### **Introduction of the Euro**

11. The Committee noted that IFAD has undertaken considerable preparation work to ensure smooth introduction of the Euro and that an expert had been engaged to review both the effects thereof and solutions relating to all aspects of IFAD's operations. Following discussions with the global custodian bank, it has been agreed to suspend trading from 15 December 1998 to ensure that all trades are settled before the end of the year. Trading in Euro will commence on 4 January 1999, when confirmation will be available of all holdings in Euro terms. An information document on this subject will be available during the Board session.

### **Other Issues**

12. The Committee received for information a status report on the implementation of recommendations contained in Price Waterhouse's report on the Review of Investment Management Activities, together with a copy of the terms of reference of the Investment Advisory Committee as approved by the President on 6 November 1998.