REPORT OF THE AUDIT COMMITTEE

1. Further to its Ninety-Second Meeting on 4 April 2006, the Audit Committee wishes to draw the attention of the Executive Board to the following matters:

2. **High-Level Review of the 2005 Consolidated Financial Statements of IFAD (AC 2006/92/R.4).** The Secretariat provided the following initial overview of the 2005 Consolidated Financial Statements of IFAD, based on the document provided (AC 2006/92/R.4)

3. The completion of the Consolidated Financial Statements of IFAD for 2005 was facilitated by the new People Soft Financial Systems and specifically the automation of the cash flow statement. Work was complicated by two factors: the application of the revision to IAS39 (the accounting standard which governs the basis of accounting for loans, receivables and certain payables) and the report on the After Service Medical Coverage Scheme (ASMCS). The latter is provided by FAO and therefore IFAD cannot complete the Financial Statements until such time as the data included within the report has been received. IFAD’s liability for the After Service Medical Coverage Scheme is substantial and Management would like to be more in control of the process in the future. As such, management would like to have our own actuarial valuation produced in the future years and have approached the World Food Programme (WFP) regarding the possibility of an IFAD-WFP joint process.

4. The Consolidated Financial Statements include information relating to IFAD, the combined Supplementary Funds, the HIPC Trust Fund, the After Service Medical Coverage Scheme Trust Fund, the Belgium Survival Fund (BSF) and the Global Environmental Facility (GEF). Although the revision to IAS 39 requires certain assets and liabilities to be recorded at fair value, data at nominal value has been included within the financial statements as it is deemed to be relevant to the users of the accounts. The high level analytical review document concentrates on these nominal values and a separate document has been prepared which reviews the impact of fair value accounting on IFAD’s results and balances.
5. Consolidated and IFAD-only Statement of Revenues and Expenses (AC 2006/92/R.4, Section A)

(a) **Income from loans (AC 2006/92/R.4, Section A (a)).** Income from loans in 2005 remain showed a slight reduction in underlying SDR terms compared to the prior year. This decrease was accentuated in USD terms by a weakening in the SDR:USD exchange rates during the year.

(b) **Income from cash and investments (AC 2006/92/R.4, Section A (b)).** Gross income from cash and investments of USD 74.6 million was USD 41.3 million lower than in the prior year. IFAD’s gross rate of return of 3.1% was below both the target rate of return of 3.5% and the prior year rate of return of 4.5%.

This is the 4th year following the change in investment policy. The remaining equity portfolio was liquidated on 1 March 2005 and invested in held-to-maturity investments, with an initial investment of USD 400 million. This investment is part of IFAD’s strategy to minimise the underlying risk of the portfolio and means that the bulk of the investment portfolio is composed of government bonds and high grade securities.

(c) **Income from other sources (AC 2006/92/R.4, Section A (c)).** In accordance with our agreement with the host government, IFAD is reimbursed by the Italian Government for certain expenditures incurred especially related to the rental costs for the Headquarters and maintenance thereof.

(d) **Contributions income (AC 2006/92/R.4, Section A (d)).** Contributions income includes complementary and supplementary contributions received from member states. The reduction in the level of contributions income in 2005, compared to 2004 is due to lower levels of complementary contributions for the HIPC DI. In 2004, contributions for HIPC totalled USD 33 million, compared to USD 4 million in 2005, a reduction of USD 29 million. In the context of the 7th Replenishment exercise, the Fund is expected to receive further complementary contributions.

(e) **Operating expenses (AC 2006/92/R.4, Section A (e)).** Operating expenses were in line with the Administrative Budget and prior year and most expenses relate to staff costs. In 2005, the new PeopleSoft Payroll System enabled IFAD to pay staff on daily contracts directly from the payroll. Underlying staff numbers increased by 2% from 2004 to 2005. Price increases reflect changes imposed by the ICSC, however the overall numbers are very much in line with prior years. 2005 saw the conclusion of the first tranche of the SCP program. The IFAD Action Plan will be included within the second tranche.

(f) **Staff salaries and benefits (AC 2006/92/R.4, Section A (f)).** The table of staff numbers by Budget Source as at 31 December 2005 shows a significant increase in the number of administrative budget staff. The increase includes 56 staff on daily temporary contracts which are included in the monthly payroll for the first time in 2005. Excluding such staff, the overall increase was less than 2%. Most of the increase in the number of staff charged under Other Sources can be attributed to the one time costs relating to the replenishment meetings which took place during the year. In addition, staff have been engaged to service supplementary funds activities and those for our hosted entities, Global Mechanism and the International Land Coalition.

(g) **Direct Charges against Investment Costs (AC 2006/92/R.4, Section A (j)).** Direct charges against investment costs were lower than last year reflecting the liquidation of the equity portfolios and reinvestment of monies into the internally managed HTM portfolio and the decrease in the value of the underlying
In addition, we received a reimbursement of the Italian tax on investments paid in prior years of approximately USD 1.5 million including retroactive interest from when the taxes were due.

(h) **Allowance for Loan Impairment Losses and HIPC Initiative Expenses (AC 2006/92/R.4, Section A (m)).** There was an increase in the allowance for the loan impairment losses principally due to a number of countries which have moved to the full provision status with arrears of more than 48 months.

In 2005, there has been a significant increase in costs relating to HIPC. The Executive Board has been fully briefed on the issue of the increasing burden of costs relating to HIPC.

(i) **Grant Expenses (AC 2006/92/R.4, Section A (n)).** Grant expenses, which are based on grant effectiveness, have increased from 2004 to 2005. In 2004, the percentage of the Programme of Work dedicated to grants increased, with a number of approvals occurring towards the end of the year. The effectiveness of these grants did not occur until 2005.

(j) **Provision for After-Service Medical Benefits (AC 2006/92/R.4, Section A (o)).** Accounting charges of USD11.1 million for past ASMCS service costs can be attributed mainly to the declining discount rate and euro-dollar exchange rate assumptions which underlie the valuation. These changes in assumptions, combined with a slight increase in the number of IFAD staff within the Scheme have resulted in an increase in IFAD’s liability.

(k) **Consolidated and IFAD-Only Balance Sheet (AC 2006/92/R.4, Section B).**

**Paragraph 41** Cash and Investments have decreased mainly due to negative exchange movements.

**Paragraph 42** Promissory Notes and Contributions Receivable Net of Provisions have decreased due to the encashment in 2005 of outstanding Promissory Notes and Receivables, mainly in relation to the 6th Replenishment.

**Paragraph 43** Net loans outstanding net of accumulated allowances for loan impairment losses and the HIPC Debt Initiative decreased USD 200 million due mainly to negative exchange rate movements.

(l) **Consolidated Cash Flow Statement (AC 2006/92/R.4, Section C).** There has been an increase in loan disbursements from USD 313.7 million in 2004 to USD 343.5 million in 2005 and a slight decrease in the loan repayments (excluding repayments made on behalf of HIPC countries). Loan repayments are expected to remain stable at their current level in future years.

(m) **Statement of IFAD-only Resources Available for Commitments (AC 2006/92/R.4, Section D).** The Advance Commitment Authority (ACA) carried forward has increased from USD 136.8 million at 31 December 2004 to USD 296.0 million at 31 December 2005 due to net outflows. In 2005, there was a net use of ACA of USD 159.2 million. This carry forward figure is within the overall ceiling permitted under the 6th replenishment resolution.

(n) **Report of the External Auditor (AC 2006/92/R.4, Section F, paragraph 61).** The work of the external auditor is complete and they will issue a clean audit opinion following the Executive Board’s authorization for issue of the financial statements.
6. **Changes in the Accounting Policy on measurement of Loans and Receivables Deriving from a Revision of International Accounting Standard 39 (AC 2006/92/R.5).**

With relation to the change in accounting policy on measurement of loans and receivables the Secretariat provided the following explanation.

7. The International Accounting Standards Board which develops the International Financial Reporting Standards (formerly International Accounting Standards [IAS]), the accounting principles followed by IFAD, has issued a revision to the accounting standard, IAS 39, which determines the valuation of certain assets and liabilities. This revision is applicable from 1 January 2005. In order to comply with IFRS, and obtain a clean audit opinion, IFAD must apply this revision.

8. In conjunction with the external auditors and their technical specialists, the Fund has undergone a lengthy exercise to comprehend the underlying concepts and application of this revision to IFAD. The Fund has also investigated the practices of the other International Finance Institutions (IFIs) to compare the application of the accounting standards (see Annex).

9. The revision to IAS 39 requires IFAD to value its loans, receivables, undisbursed grants and deferred revenues initially at fair value and subsequently at amortised cost using the effective interest method.

10. Fair value is defined as “the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm’s length transaction”. In order to calculate this fair value, management must estimate the present value of the expected future cash flows using relevant discount rates.

11. The most significant effect of this change in valuation basis is on IFAD’s loan portfolio. For loans provided on commercial terms, the fair value is almost equal to the nominal value, as the interest received compensates for the fact that future principal repayments have a lower intrinsic worth due to the time value of money. IFAD, however, provides the majority of its loans at highly concessional interest rates, with repayments over up to 40 years including an initial grace period of 10 years. The fair value of these loans is, therefore significantly lower than the nominal value originally disbursed, e.g. a loan of USD 1 million in 2005 may be worth only USD 500 000 in fair value terms, taking account of the highly concessional rate of interest, lengthy repayment period and grace period. This fair value is calculated by setting out each of the 6 monthly principal and interest cash flows over the forty year repayment period and applying a relevant discount factor to estimate the value of that future flow in today’s terms.

12. The difference between the initial fair value and the nominal value is a cost which IFAD must recognise at day one. This cost may be considered to be the grant element of the loan, given that the loan is provided on highly concessional terms. The initial cost will subsequently be amortised or clawed back over the 40 year loan repayment period (including the grace period), showing as a positive impact on IFAD’s Statement of Revenues and Expenses. This amortisation is necessary in order that the net fair value of the loan after all the repayments have been made is zero.

13. It should be noted that the amount shown in the interest income line in IFAD’s Statement of Revenues and Expenses reflects the highly concessional interest rates charged by IFAD, the additional annual positive amortisation represents the difference between this highly concessional rate of interest and interest charged at commercial rates.

14. The calculation of the fair value is performed by applying discount rates to future estimated cash flows on a loan by loan basis. The discount rates are based on forward interest curves for each year in the currency in which each individual loan is denominated. Forward interest rates are published officially by a number of sources (including Bloomberg and Reuters). However, the majority of loans are denominated in SDR and interest curves for all...
the time periods necessary (i.e. up to 40 years) are not readily available. Therefore, these interest curves had to be calculated with reference to the interest curves of each of the underlying currencies which make up the SDR (USD, Japanese Yen, GB Pound, Euro, formerly French Franc and Deutschemark), and weighted according to the formula issued by the International Monetary Fund. In addition, forward interest rates were not available for all the relevant time periods i.e. up to 40 years for these underlying currencies. In these cases, the rates were extrapolated based on those time periods which were available.

15. The discount factor is not adjusted for country credit risk as loans are considered to be “sovereign debt”. However, outstanding loans continue to be reviewed for impairment on a loan by loan basis and a provision is established where there is objective evidence that a loan is impaired.

16. As the revision is applicable from 1 January 2005, the prior year balances have not been re-stated. However, it is necessary to calculate the impact on the opening reserves of IFAD, as if IFAD had always applied fair value accounting. This is a one-off exercise. In the future, the net gain or loss in the year will be based solely on the fair value adjustment for new loans net of amortisation of loans adjusted for in previous years. As a result of this change IFAD’s opening retained earnings were reduced by USD 1.1 billion. This reduction was somewhat offset by a positive impact in the year of approximately USD 100 million, giving a net negative impact as at 31 December 2005 of USD 1 billion.

17. It should be noted that for operational purposes, IFAD refers to funds available for commitment in nominal terms. However, in order to comply with International Financial Reporting Standards, we are required to report assets and liabilities at fair value. As such we have included additional disclosure in nominal terms as it is deemed to be useful to the reader.

18. The Committee commented on the Change in Accounting Policy, and the Secretariat and the external auditor responded as follows:

(a) **Discount Rate:** The Committee expressed concerns that the discount rate used in the calculation of the fair value was more than the level of inflation for the period. The external auditor explained that inflation is not considered as part of the calculation, and that the discount rate is based on the difference between a commercial rate of interest in the market and the concessional rate of interest charged by IFAD (i.e. 0.75% in the case of highly concessional loans). The external auditor explained further that these discount rates are based on forward interest curves, and are applied to each repayment on a loan-by-loan basis, taking account of the grace period.

The impact of the revision to IAS 39 is due to the fact that IFAD provides loans on highly concessional terms. There is a cost to the Fund associated with these terms, because the future value of the loan in fair value terms is less than the nominal value of the loan at day one. This cost is measured as the difference between the interest at commercial rates and the interest actually charged by IFAD at highly concessional rates. This cost can be estimated on day one and is taken as a cost to the institution at that time. If the interest charged on the loan was equal to the market rate, there would be no difference between fair value and nominal value, and no cost to the institution.

The Committee asked for clarification as to the discount rate used in estimating the fair value. The Secretariat replied that multiple discount rates are used depending on the timing of the repayments. These discount rates are calculated with reference to forward interest curves of the underlying currencies in which the loans are denominated. The majority of loans are denominated in SDR. As the SDR is based on a basket of currencies, (GBP, USD, JPY, Euro (previously French Franc and Deutschemark)), it was necessary to calculate the SDR curves
based on the underlying currency forward curves weighted according to the IMF formula.

The Secretariat confirmed to the Committee that the source for these forward interest curves is Bloomberg, as these rates are officially published rates. In the cases where no official rates were available (for example in the earlier years), an extrapolation process was undergone based on the available information.

The Committee questioned why it was necessary to take past rates rather than future rates. The external auditor explained that given that this is a change of accounting policy, it is necessary to calculate the impact as if IFAD had always accounted for its loans at fair value. This one-off exercise therefore required reference to past forward interest curves. It should be noted that the accounting standard allows for this retrospective impact to be adjusted against opening reserves rather than being recognised during year in the Statement of Revenues and Expenses.

The Secretariat confirmed to the Committee that following this initial one off calculation, IFAD will be required to perform additional calculations each year in order to ascertain the fair value adjustment in relation to new loans.

The Committee commented that the cost to IFAD at day one is essentially equivalent to the grant element of the loans, given that they are on highly concessional terms.

(b) **Country Risk:** The Committee asked whether the calculation of fair value takes account of the risk that certain countries will not pay back their loans. The External Auditors noted that as the loans are considered to be “sovereign debt” as they provided to country governments or states, and therefore there is no adjustment to the discount rates regarding country risk. The Secretariat noted, however, that IFAD continues to review the loans for impairment on a loan by loan basis. This accumulated allowance is stated at fair value in order to be in line with the value of the related outstanding loans. Likewise, the accumulated allowance for the HIPC Debt Initiative has also been re-stated at fair value.

(c) **Future trends:** The Committee requested the Secretariat to forecast trend of the fair value adjustment in future years, also based on the experience of other comparable IFIS. The External Auditor noted that new loans will have a negative effect on IFAD’s Statement of Revenues and Expenses, however this will be offset by the positive effect of the “clawback” or amortisation of the initial cost.

(d) **Other IFIs:** The Committee requested the Secretariat to provide information regarding the application of IAS 39 (revised) by other similar IFIs. The Secretariat explained that the revision to IAS 39 was only applicable as from 1 January 2005, and therefore as yet there are no published results available. The Secretariat noted that it has been in contact with these other IFIs in order to understand their approaches but it also noted that the concessional lending arms of IFIs do not generally adhere to IFRS, but produce Special Purpose Financial Statements which are not required to comply with this revision. The Secretariat noted that IFRS are stringent and therefore highly considered within the accounting world, whilst special purpose accounts have more flexibility but are not so highly esteemed. The Secretariat subsequently produced a table (shown in the Annex to this report) setting out the accounting standards applied by other key IFIs.

(e) **UN & IPSAS:** The Secretariat noted that the UN system has recently announced that it will be moving from reporting under the UN accounting standards to
IPSAS (the International Public Sector Accounting Standards). IFAD has prepared an analysis of the impact of changing from IFRS to IPSAS, and noted that the impact would be negligible. The Secretariat, in conjunction with the External Auditors, also examined the impact of applying IPSAS rather than IFRS in the question of fair value accounting. IPSAS is, however, fundamentally based on IFRS, and in those cases where no relevant standard has yet been produced (as is the case for IAS 39), IPSAS refers users to IFRS. Therefore, IFAD would still have been required to change its accounting policy.

(f) IFRS & IFAD: The Committee commented that IFAD is not a commercial, self-sufficient enterprise and provides loans on highly concessional rates rather than market rates. As such, the Committee questioned whether it is relevant to apply International Financial Reporting Standards and the fair value measurement system. The external auditor responded that IFAD must comply with all the accounting standards if it is going to apply IFRS. However, IFAD may wish to consider whether it is appropriate to continue applying IFRS in future years.

The Secretariat noted that it had considered all the options available to it regarding the application of the revision, and would monitor this matter on an ongoing basis. It was noted that although the application of fair value accounting is not deemed to be relevant to the institution, it was important to obtain a clean audit opinion to demonstrate that IFAD complies with best practice in financial reporting.

19. The Committee commented on the High-level Review, and the Secretariat and the external auditor responded as follows:

(a) Fair Value: The Committee drew attention to the impact of the change in accounting policy which was then discussed in detail under agenda item AC 2006/92/R.5.

(b) Investment Income: The Committee noted the lower levels of income in 2005 compared to 2004 and requested information on potential future trends. The Secretariat noted that in 2005, IFAD received technical comments from the World Bank in its role as financial advisor to the Fund, regarding the performance of the investment portfolio and its levels of risk and with the assistance of the World Bank is aiming to find a better solution to help improve results for this year.

On 31 March 2006, the World Bank submitted its final comments to the Fund on the expected rate of return based on different asset allocation scenarios, and management is in the process of analysing these comments and evaluating alternatives for the Fund.

(c) Contributions Income: The Committee pointed out the lower levels of income in 2005, compared to 2004. The Secretariat explained that the main reason for the reduction was lower complementary contributions for the HIPC Debt Initiative of approximately USD 29 million.

(d) Expenses: The Committee expressed their concern at the increasing level of expenses, especially in the light of lower income in 2005, indicating that IFAD is heavily reliant on its Replenishment resources. Assurances were given that the Fund carefully monitors expenditures, and that the level of costs has been closely reviewed as part of the 2006 budget process.

(e) Staff numbers (paragraph 16): The Committee highlighted the increase in the number of administrative staff from 2004 and 2005 and requested some clarification of the table disclosed. The Secretariat explained that the table showed the number of staff whose costs are charged to the different budget
sources. The increase in the number of staff charged to “other sources” was due to staff charged to “one time costs” as a result of the Replenishment meetings. This budget source included staff for SCP and staff engaged for activities relating to the hosted entities (Global Mechanism and the International Land Coalition). It should be noted that the hosted entities provide a contribution towards the cost of services which IFAD provides. The Secretariat also drew attention to the fact that the 2005 figures include 56 staff on daily contracts, previously paid manually and as from 2005 included within the automated payroll system.

(f) **Direct charges against investment costs:** The Secretariat confirmed to the Committee that in 2005, the Fund had received, in full, reimbursement of the Italian tax receivable referred to in prior years.

(g) **HIPC DI costs:** The Committee requested clarification on the high level of costs in 2005 and its implications on IFAD’s core function. The Secretariat agreed that the cost of HIPC is high, but that the Executive Board is kept fully informed of these costs, and that each country must be approved by the Board before it can receive relief. The Secretariat confirmed that it is continually monitoring the growing cost of HIPC to IFAD and noted that it is trying to obtain access to the World Bank’s Trust Fund, in order to reduce the burden of these costs, which the Committee supported strongly.

(h) **Net Loans Outstanding versus Contributions:** The Committee noted that the net loans outstanding of USD 3.6 billion were lower than the total contributions of USD 4.6 billion. The Secretariat commented that contributions are equivalent to a company’s share capital, of which the major part used for funding loans and grants, being IFAD’s operations. Some resources are used for operating budgets, although historically investment income has covered the administrative budget. The net loans outstanding represents disbursements net of repayments to date and does not include commitments for future loans and grants not yet disbursed. Therefore, it is normal that loan outstanding is lower than the contributions. In addition, it was noted that IFAD has USD 1.5 billion of fully committed retained earnings and a general reserve of USD 95 million. The Committee noted that these positive retained earnings showed that historically IFAD’s revenues have exceeded their costs.

(i) **Appendix G to the Financial Statements:** The Committee noted that Appendix G to the Financial Statements was stated in SDR, rather than USD. The Secretariat explained that Appendix F Statement of Loans, is also stated in SDR as the loans are denominated in SDR, and therefore the HIPC related portion of the loans is denominated in SDR, showing the underlying currency of the commitments. However, the USD equivalent is disclosed in both Statements F and G.

20. **Review of the Audited Financial Statements of IFAD for 2005 (AC 2006/92/R.3).** The Committee has reviewed the Audited Financial Statements of IFAD for the year ended 31 December 2005. The Audit Committee endorses these statements and the Executive Board will submit the statements to the Thirtieth Session of the Governing Council, in accordance with the Regulation XII (6) of the Financial Regulations of IFAD.

21. The Committee commented on IFAD’s 2005 Consolidated Financial Statements, and the Secretariat and the external auditor responded as follows:

(a) **Appendix G Summary of Debt Initiative for HIPC countries:** The Committee requested clarification of the HIPC disclosures. The Secretariat explained that following the approval by the World Bank that a country has reached Decision Point, IFAD takes its share of the debt relief as a cost.
The Secretariat noted that 2 or 3 countries are due to reach decision point in 2006, and therefore the costs relating to IFAD’s share of these countries’ debt will be charged in 2006, assuming approval by the World Bank and the Executive Board. In addition, it was noted by the Secretariat, that HIPC is a subjective area as the nominal costs are calculated as a function of the Net Present Value approved by the Executive Board and based on a number of assumptions. Changes to these underlying assumptions (in relation to dates, exchange rates and disbursement levels) are charged through the Statement of Revenue and Expenses.

The Committee requested the Secretariat to indicate whether HIPC would continue to increase in future years. The Secretariat noted that to date, 27 countries have been approved to receive debt relief from IFAD. A further 10 countries are set to reach decision point in the next few years and as such will create additional costs for IFAD. As shown in Note 11 of Appendix H to the Financial Statements, the costs associated with these countries are estimated to be USD 179 million, as at 31 December 2005. In addition, the interest portion of the debt relief provided by IFAD on behalf of the HIPC countries is charged to the Statement of Revenue and Expenses as it falls due. Therefore, as long as payments continue to be made on behalf of HIPC countries, there will be an annual charge.

The Secretariat confirmed to the Committee that the Debt Sustainability Framework had been approved by the Executive Board.

(b) Pension Fund (AC 2006/92/R.3 Appendix H, Note 7b): The Committee requested clarification regarding the risks associated with the pension fund. The Secretariat explained that IFAD employees are part of the UN Joint Staff Pension Fund, for which an actuarial valuation is performed every two years. The latest available report is at 31 December 2003 which showed an actuarial surplus, as shown in the financial statements. The next valuation is due for the period ended 31 December 2005, and the results are not expected until June 2006. As IFAD is part of the group plan, it does not have control as to the reporting timetable of the results. The Secretariat noted that the pension fund has experienced both gains and losses in the past, however, in the case of a deficit, historically the UN organisations have never been required to make good such a deficit. In the case of continued deficits, the level of contributions has instead been increased. The Secretariat therefore considers that it is unlikely that IFAD will ever be requested to make a one-off payment. IFAD has 3 representatives on the UN Pension Fund Board and therefore takes an active part in discussions.

The Secretariat confirmed that the pension fund is a defined benefit scheme. Staff and IFAD itself are required to contribute a fixed percentage of each staff member’s pensionable remuneration, monies which are subsequently invested by the fund until retirement. This fund is entirely separate from IFAD.

The Committee proposed that the Secretariat provides more information when the latest actuarial valuation is received.

(c) Net Loss in 2005: The Committee commented that the net result for the year was a loss of USD 450 million. The Secretariat noted that for operational purposes, Appendix D Statement of Resources Available for Commitment is a more relevant source of information as it provides information regarding the resources available to commit for additional loans and grants. In fact, the retained earnings are fully committed for loans and grants and as at 31 December 2005, there has been a net use of the ACA. IFAD records its results in order to comply with accounting standards. The net loss is due mainly to exchange rate
losses due to the fact that IFAD reports its results and balances in USD, whilst the loans are denominated in SDR. IFAD provides an SDR balance sheet (Appendix B1) in order to show that the assets have actually increased slightly from 2004 to 2005. The external auditor confirmed that the exchange loss is due to the fact that IFAD reports using USD rather than SDR, i.e. it is an accounting loss. He also noted that IFAD should continue to monitor the HIPC costs, but that it is necessary to look at IFAD from a strategic, long term point of view, rather than one year’s results.

22. **Internal Audit Activities and Plans (AC 2006/92/R.6).** This Committee considered the activities during 2005, the Strategic Directions and Planned activities for 2006 and the findings of the review of the implementation of the internal audit recommendations which were conducted in February 2006.

23. **IFAD Anti-Corruption Policy.** The Committee Members recalled that the Anti-Corruption Policy and the related Action Plan were approved by the Executive Board in December 2005 (document EB 2005/85/R.5/Rev.1 refers). Since then, the Fund has undertaken the implementation of the comprehensive Action Plan linked to the Anti-Corruption Policy. An Anti-corruption web-site was also created and can be accessed through the IFAD official Web-Site www.ifad.org.

24. **The Oversight Committee** was reported to have had a slightly reduced investigation caseload in 2005; however the anti-corruption awareness activities necessitated extensive time involvement of the Senior Internal Audit Staff Members. Such activities included the issuance of the first annual report of the Oversight Committee (OVC) and the presentation of the report to all IFAD staff through divisional meetings.

25. **Risk Management.** Also under the coordination of the Office of Internal Audit, the Risk Management Mechanism was incorporated into the IFAD Strategic Planning Process. This initiative was carried forward to 2006 with the definition of a risk management strategy for the IFAD Action Plan.

26. **Implementation of Internal Audit Recommendations (AC 2006/92/R.6 Section V, paragraph 23).** Tables 4 and 5. Committee Members noted that in comparison to the Internal Audit Activities of 2005 no major activities were foreseen for 2006. It was explained that in-fact there were no major policy initiative planned for 2006. However, the implementation of the anti-Corruption policy will constitute a major OA responsibility in 2006 with 142 working days allocated for this activity. These implementation activities include all the elements in the anti-corruption Action Plan. The Committee will report to the Executive Board in 2007 on the state of progress of this Action Plan.

27. **Status of Implementation of the Internal Audit Recommendations Table 4.** The number of recommendations implemented rose in number by 89 for a total of 449 as many recommendations that were previously “in progress” were completed. The large reduction of the “in-progress” recommendations can also be attributed to the stance adopted by OA in 2006, whereby no real progress is made for some time then the recommendations are downgraded to the “incomplete” or “no progress” statuses. These two categories constitute a sub-total of 72 recommendations in the “Requiring Improvement” group. The number of pending recommendations declined from a total of 312 in 2002 to 230 in 2005, however the length of time which the remainder have been outstanding has increased by 7 months in 2004 to 38 months.

28. **Implementation Status of Recommendations by Functional Category (as at 31 December 2005) Table 5.** Further clarification was sought for the recommendation which required improvement in the HR and Consulting area, in particular the outstanding implementation of a Consultants’ Roster. The Committee was informed that although the recommendation for a Consultants’ Roster has been on-going for the past five years, the delay in this project’s completion can be partially attributed to the heavy involvement of the Human
Resources Office in activities such as participation in the ICSC Pay for Performance Pilot Programme, the issuance of the Human Resources Procedures Manual (HRPM) and the development of the new PeopleSoft Payroll System.

29. **Table 5** also indicates that the progress in implementing recommendations can be noted in the areas of Finance and Accounting with a total of 94 recommendations now implemented and Human Resources and Consultants with 47. The table also shows the split of the 72 recommendations “Requiring Improvement”. The area of “Human Resources and Consultants” has the highest proportion of recommendations in this status at 23%.

30. Clarification was also sought on the results of the audit on the administration of workshops. The Office of Internal Audit responded that the main recommendation related to the more extensive use the streamlining tools which are available to the organizers, more specifically:

- The use of Special Service Agreements which facilitate the hiring of local staff at more economical rates;
- Make better use of group travel arrangements
- Better involvement of the Conference Services Office and of their expertise.
- Establishment of official procedures in coordination the Office of the Secretary for the organization of workshops and meetings.

31. The Committee raised a concern on the high percentage of OA staff time in 2005 devoted to Office Management and Capacity Building (32%). OA acknowledged that this percentage is high but explained that this was mainly due to extraordinary and necessary capacity building activities undertaken in 2005 and was seen as an “efficiency investment” which is already producing results. It is foreseen that the 2006 figures will decline significantly in this area, while the efficiency and quality gains will increase. The specific areas of the capacity building are indicated as:

- Introduction and training of electronic audit working papers, audit management and time reporting software
- Creation of a comprehensive manual which reflects investigation and advisory activities
- Re-organization of the Unit’s objectives and their reflection in the staff’s post descriptions
- Recruitment of two new staff members for the Investigations area

**Recommendation**

32. The Audit committee recommended the endorsement of the IFAD Financial Statements for 2005 by the Executive Board for presentation to the Thirtieth Session of the Governing Council.
## REVIEW OF ACCOUNTING STANDARDS FOLLOWED BY OTHER IFIs/ PEER ORGANISATIONS

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<th>Entity</th>
<th>US GAAP</th>
<th>IFRS</th>
<th>Special purpose</th>
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<td>International Finance Corporation</td>
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<td>Asian Development Bank</td>
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<tr>
<td>➢ Nigeria Trust Fund</td>
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<td>➢ African Development Fund</td>
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<td>Inter-American Development Bank</td>
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<td>➢ IADB</td>
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<td>Special Purpose: in compliance with Agreement Establishing the IADB</td>
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<tr>
<td>➢ Other Trust Funds</td>
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<tr>
<td>➢ Fund for Special Operations</td>
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<td>No fair value accounting or impairment for loans was presented by the fund, hence a qualified audit opinion was issued by the External Auditors.</td>
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