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IFAD

INTERNATIONAL FUND FOR AGRICULTURAL DEVELOPMENT

Executive Board – Eighty-eighth Session

Rome, 13-14 September 2006

REPORT OF THE AUDIT COMMITTEE

For: Approval

REPORT OF THE AUDIT COMMITTEE

1. At its ninety-third meeting, held on 11 September 2006, the Audit Committee discussed the following matters which it wishes to bring to the attention of the Executive Board.
2. **Nomination of the new Chairperson of the Audit Committee.** In accordance with the procedures for the appointment of members to the Audit Committee (EB 2006/87/R.33), members were invited to elect a Chairperson, whose term would end in April 2009. In response to a proposal made by the representative of the United States of America, the Committee unanimously elected the representative from Italy, Mr Augusto Zodda, as Chairperson.
3. **Adoption of the agenda (AC 2006/93/R.1).** The agenda was adopted without change.
4. **Minutes of the ninety-second meeting of the Audit Committee (AC 2006/93/R.2).** The minutes were approved without change.
5. **Report of the external auditor on internal control and accounting procedures (AC 2006/93/R.3).** The Committee noted that the external auditor had identified a number of areas in which controls should be strengthened on a high-priority basis and, in the light of these recommendations, requested clarification of the overall adequacy of IFAD's procedures and controls. The external auditors confirmed that they considered IFAD's general control environment to be more than reasonable. Although the report identified some weaknesses to be addressed with high priority, the external auditor confirmed that these weaknesses did not represent fundamental errors or mistakes such as to undermine the accuracy of IFAD's financial statements, which were issued with a clean audit opinion, and suggested that implementation of the recommendations relative to them should be subject to consideration in cost-benefit terms to the Fund. The Committee underscored the importance it attached to the recommendations regarding the timing of the delivery of the actuarial report of the After-Service Medical Care Scheme (ASMCS) and the current limits of the Loans and Grants System.
6. **Review of the external auditor's proposal and approval of the programme of work for 2006 and related fees (AC 2006/93/R.4).** The Committee requested clarification on the reason for the increase in the 2006 audit fees to EUR 132,000, an increase of 14.8% over the previous year. It was explained that the increase was related to the additional costs to be incurred by the external auditor, especially in relation to the recurring work required under the new international financial reporting standard (International Accounting Standard 39). The 2006 fee would cover all such costs on an ongoing basis. The Committee agreed to nominate PricewaterhouseCoopers for appointment by the Executive Board as external auditor for the 2006 financial statements and to approve the audit fee of EUR 132,000.
7. **Policy on rotation and on services to be provided by the external auditor (AC 2006/93/R.5).** The Committee noted that IFAD had retained the same external auditing firm, PricewaterhouseCoopers, for 28 years. The secretariat pointed out, and the Committee acknowledged, that PricewaterhouseCoopers had provided high-quality service. The Committee discussed the implementation of a mandatory rotation policy, in line with many other major international financial institutions (including the World Bank and Inter-American Development Bank). The Committee suggested a maximum of two five-year terms for the external auditor, mandatory rotation of the engagement partner and exclusion of the provision of any other services. The secretariat was asked to prepare a proposal on a rotation policy – in line with the aforementioned suggestions – for discussion at the next meeting of the Committee and subsequent presentation to the eighty-ninth session of the Executive Board in December 2006.
8. **Oversight Committee report for 2005 (AC 2006/93/R.6).** In comparison with the 2004 Oversight Committee report (which was the first one presented to the Audit Committee), the Audit Committee found that the 2005 report was less detailed and did not provide a scale of severity for the

cases submitted. The Director of the Office of Internal Audit indicated that the report reflected the nature of the cases identified as well as the Fund's policy to protect the identities of both whistle-blowers and the subjects of any allegations. The secretariat assured the Audit Committee that future reports would include a more comprehensive account of investigations and a section on lessons learned. The next report would be issued in April 2007.

9. **Project audit status report for 2004 (AC 2006/93/R.7).** This report had originally been presented to the Audit Committee in November 2005 but there had not been time to discuss it. The report was therefore resubmitted to the September 2006 meeting of the Committee in accordance with the requirement to supply an annual report on the status of project audits. The secretariat noted that all 2004 audit reports had since been received. The benchmark date for the status of 2005 project audits was set at 30 September 2006. The Committee highlighted the need for future reports to contain additional information on the quality and content of the project audit reports submitted and on the status of the implementation of audit recommendations. The secretariat stressed that the primary responsibility for the monitoring and follow-up of project audit reports lay with the cooperating institutions, and noted that more in-depth analysis and reporting could have an impact on the level of resources required. Following the Committee's comments, the secretariat agreed to further develop the content of the project audit status report for 2005 that is expected to be submitted to the Audit Committee in December 2006.

10. **Selection of the external auditor of IFAD for the period 2007-2011 (AC 2006/93/R.8).** In the light of the discussion of the policy on rotation and on services to be provided by the external auditor, the Committee requested clarification on the legal implications and status of the present tender process. The Office of the General Counsel stated that IFAD had not yet entered into an agreement with the winning bidder, which required approval by the Executive Board, and accordingly it was not legally bound. However, it was noted that the tender process was in the final stage, and it would not be possible to substantially modify the terms of reference without retendering or seeking a clarification. As a result of the discussion, the Committee recommended that the current tender process be concluded. In line with the management recommendation, PricewaterhouseCoopers would be nominated to the Executive Board for appointment as external auditor. At the same time, a new policy on auditor rotation and services to be provided by the external auditor would be defined according to the discussion reported above in paragraph 7.

11. **Discussion on the terms of reference of the Executive Board and Audit Committee regarding financial policy.** Following an open exchange of views, the Committee concluded that there was no pressing issue of financial policy that might require it to give special and additional assistance to the Executive Board. The Committee further recognized that its role in this area should respond to requests from the Executive Board in the discharge of its responsibilities with regard to investment policy pursued by the President, as governed, inter alia, by regulation VIII of the Financial Regulations of IFAD. In this respect, the Committee expresses to the Executive Board its availability to provide, on request, analysis or review in this area, within the scope of its terms of reference.

12. **Other business.** In accordance with the decision taken by the Executive Board at its eighty-seventh session in April 2006, the Audit Committee should continue to review the Fund's annual budget prior to its submission to the Board. Accordingly, the terms of reference of the Audit Committee, which have been revised, are attached hereto.

ATTACHMENT

TERMS OF REFERENCE OF THE AUDIT COMMITTEE

The role of the Audit Committee is to assist the Executive Board in exercising control over the financial administration of the Fund. To this end, the Committee will:

- (a) Review the draft annual financial statements.
- (b) Nominate the external auditor to the Executive Board, following a review of the scope, costs and contractual terms of the appointment.
- (c) Review the detailed scope, design and results of the audit in private sessions with the external auditor (as now, but more explicit).
- (d) Satisfy itself that the recommendations of the external auditor are promptly acted on by Management.
- (e) Commission special investigations from the external auditor where it sees fit.
- (f) Every five years, review the case, from first principles, for rotating the appointment of the external auditor.
- (g) Satisfy itself that the internal audit function is effective and efficient, and that audit reports are promptly acted on by Management.
- (h) Review the application to the Fund of new or revised accounting standards and principles.
- (i) Conduct a triennial review of the level of the General Reserve.
- (j) Conduct a triennial review of the risks faced by the Fund and its risk-management procedures, satisfying itself, *inter alia*, that the internal control and risk-management systems established by Management in the areas of investment and procurement effectively safeguard the Fund's assets.
- (k) Report to the Executive Board on any matters arising from the above terms of reference and submit such conclusions and recommendations thereon as the Committee deems appropriate.
- (l) Examine in November the budget document to be submitted to the December Board session and prepare a report to that same session containing an account of its meeting.
- (m) Undertake other tasks, within the scope of the above terms of reference, remitted to it by the Executive Board.