REVIEW OF IDA INTERNAL CONTROLS
An Evaluation of Management’s Assessment and the IAD Review

Volume III
Report on the Completion of Part II
IMPROVING DEVELOPMENT RESULTS THROUGH EXCELLENCE IN EVALUATION

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Review of IDA Internal Controls

An Evaluation of Management’s Assessment and the IAD Review

Volume III

Report on the Completion of Part II
Final Report on the Effectiveness of IDA Internal Controls for Assuring Reliable Financial Reporting, Compliance with IDA’s Charter and Policies, and Operating Efficiency and Effectiveness

Attachments

This paper is available upon request from IEG-World Bank.

2009

The World Bank
Washington, D.C.
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Management’s Overall Assessment
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<td>Analytic and Advisory Activities</td>
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<td>Africa Region</td>
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<td>Annual Review of Development Effectiveness</td>
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<td>Annual Report on Portfolio Performance</td>
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<td>Bank</td>
<td>IBRD sometimes together with IDA</td>
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<td>Abbreviation</td>
<td>Full Form</td>
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<td>Procurement Specialist /Procurement Accredited Specialist</td>
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Executive Summary

1. As set out by the Commission of Sponsoring Organizations of the Treadway Commission (COSO), under the COSO internal controls framework, Management is responsible for establishing and maintaining an effective internal control system. IDA’s management has assessed internal control over IDA’s operations, and based on this assessment, and reflecting the work undertaken by management, and attested to by the external auditor, during the FY07 ICFR process, management is of the view that the internal control system over IDA’s operations is adequate to provide reasonable assurance to Senior Management and the Executive Directors that:

- IDA’s published financial statements are being prepared reliably;
- IDA carries out its operations in compliance with the relevant provisions of its Articles of Agreement and operational policies and procedures including provisions relating to the use of funds for intended purposes; and,
- They are made aware, in a timely manner, of the extent to which IDA is moving toward effective and efficient use of its resources in meeting its operational objectives.

2. Significant deficiencies. As part of its assessment, however, management has identified a number of significant deficiencies which require remedial actions—and effective monitoring of their implementation—in order to strengthen the internal control system over IDA’s operations. These significant deficiencies, described below, fall into five categories: (a) Investment Lending (IL) framework; (b) controls for managing fraud and corruption risk that may be associated with IDA-supported operations; (c) oversight of Procurement (PR) and Financial Management (FM) work related to IDA-financed projects; (d) identification of systemic risks; and (e) Analytic and Advisory Activities (AAA) and Information Technology (IT) issues:

   (a) Issues relating to the current policy and procedural framework for IL:

   o Process inefficiencies, including a lack of focus on key risks and controls during preparation/design and supervision stages of IL projects.
   o Outdated and complex policy framework for IL as reflected in multiple OPs and BPs that apply to IL operations.
   o Risk identification and reporting with an emphasis on information-sharing within the task teams and between staff and management during project supervision, including diffused accountability in such areas.
   o Timely accessibility of operational documents primarily relating to IL operations.

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(b) **Issues relating to Integration of Controls for Managing Fraud and Corruption Risk in IDA-supported operations:**

- Need for better design and integration of controls for managing fraud and corruption risks (reflecting, inter alia, lessons learned from precedents and INT work) into design/preparation and supervision/monitoring of IDA-supported operations.

(c) **Issues relating to PR and FM:**

- Adequacy of controls in place to ensure consistent follow-up on PR issues by the task teams, including the need for better integration of PR staff in task teams and clarification of accountabilities for procurement issues and decisions.
- Inconsistent implementation of PR post-reviews.
- Inconsistency in quality arrangements for the documentation of FM supervision and some inconsistency in quality arrangements for oversight and monitoring of FM supervision.

(d) **Issues relating to identification of systemic risks**

- Inadequate mechanisms for risk aggregation and timeliness and consistency in monitoring, identifying (and formulating an appropriate response to) systemic risks.

(e) **Other Issues:**

- AAA processes and controls.
- IT controls relating to password sharing in SAP, privileged access, and Infrastructure Change Management.

3. Management has formulated specific recommendations to address the above significant deficiencies through monitorable actions. Several of these actions are already in place; others are underway and management is committed to implementing them over the next 12-18 months and reporting to Senior Management and the Executive Directors on the results achieved, including through periodic progress reports (with the first one being prepared in the early fall of 2009 in time for the IDA 15 mid-term review). The recommended actions fall within six areas:

- **IL reform**, expected to: (a) improve IL instrument efficiency and effectiveness, (b) rationalize and strengthen control framework for IL by adopting a risk-based model to appraisal and supervision of IL operations, (c) eliminate current backlog of outdated OPs and BPs by creating a principles-based umbrella policy for IL operations; and (d) align incentives and accountabilities to facilitate more timely risk identification, reporting and information-sharing within the task team and between management and staff.

- **Better design and integration of controls for managing fraud and corruption risks** into design/preparation and supervision/monitoring of IDA-supported operations, expected to strengthen the Bank’s ability to detect, deter and address, in partnership with country counterparts, issues of fraud and corruption and form part of the GAC implementation plan and follow-up actions to the Volcker Panel Report and the India DIR Report.
• **Strengthening quality arrangements in the PR and FM areas**, by raising awareness and achieving better integration of fiduciary staff in task teams and re-clarifying accountabilities within the task team for fiduciary issues generally and oversight of contract management in particular; and strengthening regional and overall monitoring of quality arrangements in the PR and FM areas, particularly during project supervision.

• **Review and improvement of mechanisms for identification of entity-wide risks**, including management’s review of QAG and adoption of an annual Integrated Risk Report.

• **IT strengthening**, expected to address password and access issues, improve compliance monitoring through automation of operational processes starting with IL, and address current issues with filing and accessibility of operational documents.

• **Improving AAA work** by simplifying and rationalizing processes and systems for the wide scope of AAA activities and strengthening compliance with this new improved framework.
I. Introduction

1. **Background.** As reflected in the IDA 14 Replenishment Report, Management committed to carry out, during the period of IDA 14, an independent comprehensive assessment of its control framework including internal controls over IDA operations and compliance with its charter and policies, and making such assessment available to the public after its disclosure has been approved by IDA’s Executive Directors. The assessment has been conducted in the context of the internal control framework developed by COSO, adapted to fit the unique nature and operations of IDA. It has been carried out in three tiers: Management self-assessment; Independent Audit Department (IAD) review; and an independent evaluation of both by the Independent Evaluation Group (IEG). The assessment has been divided into two parts: Part I, which focused on design and operating effectiveness of controls over IDA operations at the transaction level; and Part II, which focused on (a) entity-level controls, (b) outstanding transaction-level controls deferred from Part I, and (c) the operations objective of COSO. The final IEG report on the results of the assessment is expected to be disclosed by IEG after it is discussed with the Audit Committee (AC) and Committee on Development Effectiveness (CODE), following in this regard usual practice relating to disclosure of IEG reports.

2. **Benefits of this exercise.** In management’s view, this has been an important and useful exercise. It enabled management for the first time to take a comprehensive look at internal control system over IDA’s operations, focusing on management and business processes conducted at transaction and entity levels across IDA. It also allowed management to assess mechanisms in place to monitor and adjust these processes to respond to identified risks and support IDA’s strategy and priorities as they evolve in response to client needs. Being the first of its kind, this assessment was much more time and resource consuming than originally anticipated at all levels and for all assessment participants (management, IAD and IEG). Building on the extensive experience and comprehensive tools and methodologies developed in the context of this assessment, management expects to mainstream a periodic assessment of internal control over IDA and Bank operations into its ongoing corporate monitoring and control functions. Further, periodic assessment of internal control will become an integral and important part of the ongoing corporate monitoring and control functions.

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1 See, Report from the Executive Directors of the International Development Association to the Board of Governors, Additions to IDA Resources: Fourteenth Replenishment, Working Together to Achieve the Millennium Development Goals, (approved by the Executive Directors of IDA on March 10, 2005), paragraph 39, under the Disclosure bullet.

2 COSO published a report in 1992, “Internal Controls – Integrated Framework,” which is widely referred to by leading financial institutions in the United States and is also seen as a model in many other parts of the world. IDA adopted the COSO framework as its controls methodology in 1995. The framework is an all encompassing process which covers all aspects of internal control of an organization’s operation. It considers not only the evaluation of formal controls, but also informal controls, such as ethics, trust, communication, organization behavior and leadership, and incorporates “top-down” as well as “bottom-up” analysis.
IDA: INTERNAL CONTROLS REVIEW: MANAGEMENT ASSESSMENT FY08

3. **Objective and structure of this report.** This report sets out management’s overall assessment, together with findings and recommendations, regarding the effectiveness of the current internal control framework over IDA’s operations. It builds on and reflects management’s assessment of effectiveness of internal control over the three objectives categories within the COSO integrated controls framework, namely: reliability of financial reporting, compliance with laws and regulations, and effectiveness and efficiency of operations. Management’s assessment, findings and recommendations relating to:

- the first objective—reliability of IDA’s financial reporting—reflects the work undertaken by management and attested to by the external auditor during the FY07 ICFR process.
- the second objective—compliance with applicable laws and regulations—reflects management’s assessment of compliance at the transaction-level (the focus of Part I, as supplemented with additional transaction-level work completed during Part II) and at the entity-level (conducted as part of the assessment of the entity-level controls during Part II).
- the third objective—effectiveness and efficiency of IDA’s operations—was the focus of entity-level work conducted during Part II and builds and reflects Part I findings relating to efficiency and effectiveness at the transaction-level.

4. Following this introduction, Section II of the report sets out a summary of scope and methodology followed by management in conducting its assessment. Section III sets out management’s overall assessment regarding the effectiveness of the current internal control framework over IDA’s operations, followed by a discussion of significant deficiencies identified by management and recommended actions to address them3. Annexes provide additional information: *Annex A* contains *Management’s Assessment of Entity-Level Controls over IDA’s Operations*, conducted during Part II of this exercise; *Annex B* sets out *Management’s Supplemental Report on Transaction-Level Controls*, which reflects management’s assessment of quality arrangements over financial management and procurement work in the context of IDA operations, mapping of AAA processes and an assessment of compliance with these processes, and supplemental work on several other modules, including the safeguards risk management process, and IDA allocation model; *Annex C* sets out the scoping memorandum for Part II of this assessment.

II. Scope and Methodology Summary

5. Throughout this assessment, and in preparing this final report, management—followed the COSO definition of internal control, namely, a process affected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in three COSO categories: financial reporting, compliance and operations. Management assessed internal controls related to these three objectives categories against different expectations, an approach that was consistent with COSO. In the context of financial reporting and compliance objectives, which are primarily within IDA’s own control, management assessed whether IDA’s internal control system can be expected to provide

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3 Please note that this overall management report reflects findings and recommendations that combine both transaction-level and entity-level work. As such, while it builds on the recommendations reflected on Annexes A and B, some of these recommendations have been prioritized and updated to reflect subsequent actions which are now in place.
reasonable assurance that IDA’s financial reporting is reliable and that IDA carries out its operations in compliance with its charter and operational policies. In the context of operations objective, however, which is not always within an entity’s control, management assessed whether the internal control system in place provides a “reasonable assurance only that management and, in its oversight role, the Board, are made aware, in a timely manner, of the extent to which IDA is moving toward its operations objectives.” It is important to note that this distinction was not reflected in management’s Scoping Memorandum for Part II, which set the operations objective in terms of “assessing whether internal controls over IDA operations provide reasonable assurance to senior management and the Board that IDA’s operations are carried out efficiently and effectively.” Management determined the need for this revision upon a closer review of the COSO report which it used to guide its entity-level work. As explained in the COSO Report, since the operations objective is not always within the entity’s control, the internal control system cannot provide an “absolute reasonable assurance” in this area the way it is expected to do with respect to financial reporting and compliance components; instead, all the internal control system can provide with respect to operational objective is a "reasonable assurance... that management and, in its oversight role, the Board, are made aware, in a timely manner, of the extent to which an entity is moving towards its operations objectives." This is especially important for IDA, given the many factors outside IDA’s control that may and often do affect the development outcomes and effectiveness of IDA’s operations. Since this review is likely to become a precedent and set standards for similar work inside and outside IDA for assessing operations objectives against the COSO methodology, it is all the more important to ensure that efficiency and effectiveness of operations is measured against realistic rather than absolute expectations, in line with the COSO approach.

6. Following is a summary of the scope and methodology followed by management in assessing each of the three objectives against these expectations.

1. Reliability of financial reporting relating to IDA’s operations

7. Since 1997, Management has annually asserted and received attestations from the external auditor that it maintains an effective system of internal controls over external financial reporting for both IBRD (International Bank of Reconstruction and Development) and IDA. The work undertaken by management, and attested to by the external auditor, during the FY07 ICFR process is described in the annexes to Management’s assertion and the external auditor’s attestation for FY07.

2. Compliance with applicable laws and regulations

8. The corporate entities for which the COSO framework was developed are subject to specific laws and regulations in their respective jurisdictions. IDA’s status as an international organization with immunities and privileges makes this COSO category not directly applicable. However, in addition to its charter (i.e. its Articles of Agreement) IDA has a body of internally generated policies and procedures with which it needs to comply. Management has therefore interpreted compliance with laws and regulations to mean compliance with IDA’s (a) Articles of Agreement, and (b) operational policies and procedures.

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9. Management’s assessment of IDA’s compliance with relevant provisions of its Articles of Agreement and operational policies and procedures was carried out in two parts. During Part I management focused on transaction-level controls relating to compliance with (a) provisions of the IDA Articles of Agreement, as interpreted from time to time by IDA’s Executive Directors, relating to the management of IDA’s lending operations, including provisions relating to the use of funds for intended purposes; and (b) internal operational policies and procedures relating to the management of IDA’s lending operations. The results of this assessment are set out in management’s Part IB report. During Part II, management also assessed entity-level controls relevant to compliance with the Articles of Agreement and operational policies and procedures linking these to the transaction-level controls relating to compliance identified and assessed under Part I (as supplemented by the additional transaction-level work completed during Part II and set out in Annex B to this report).

10. Detailed methodology and scope for carrying out the compliance assessment at the entity-level is set out in Management’s Part II Report (attached as Annex A). The tools utilized in carrying out this assessment include: (a) preparation and assessment of entity-level questionnaire (the “ELC questionnaire”) answered by all vice presidents and stand-alone directors, and managing directors as of September 2007; (b) review and assessment of the terms of reference, key outputs (including main recommendations in the most recent reports) of IDA’s central control groups, including documentation and review of the current budget process; (c) review of IDA’s general computer controls related to its information technology; (d) review of decentralized operations using IAD’s country office program audits; and (e) assessment of the Board’s function. In accordance with document sharing process adopted under Part I, all documentation and testing results relating to the above were provided to IAD and IEG for their review and evaluation, respectively.

11. Management believes that the sequencing of the compliance assessment, which commenced with the “bottom-up” approach during Part I to assess compliance at the transaction-level, was necessary in light of the nature of the commitment made under IDA 14, namely to specifically review compliance with applicable charter provisions and policies in place. By focusing during Part I on transaction-level controls relevant to compliance with IDA charter and policies, management was able to identify and test key management and business processes that apply to IDA’s lending operations and bring out the crucial details of operational compliance and any issues that affect operational efficiency and effectiveness (like inefficiencies of current “one-size-fits-all” processes for IL projects and tools in place to assess progress and effectiveness of operations. The more conventional approach of commencing this work with entity-level controls5 may have been less time and resource-consuming. However, in management’s view the overall results of management’s assessment show that this alternative methodology would not have yielded the same depth, specificity and relevance of findings and actionable recommendations as was made possible through the sequencing of assessment work undertaken and the methodology adopted by management.

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3. Effectiveness and efficiency of IDA’s operations

12. Part II of management’s assessment has focused on whether internal controls over IDA operations provide reasonable assurance to Senior Management and the Board that they are made aware, in a timely manner, of the extent to which IDA is moving toward effective and efficient use of its resources in meeting its operational objectives.\(^6\) The transaction-level assessment under Part I yielded important findings that had a significant bearing on, and were reflected in, the overall assessment of internal controls over effectiveness and efficiency of operations. The findings and recommendations of this assessment, and the detailed methodology and scope for carrying it out, are set out in management’s Part II report (attached as Annex A).

13. In summary, the main tools utilized by management in carrying out an assessment of entity-level controls relating to efficiency and effectiveness of operations included:

- preparation and assessment of the ELC Questionnaire that addressed the five COSO components (control environment, risk assessment, control activities, information and communication, and monitoring and evaluation) as well as anti-fraud and corruption controls;
- assessment of the Board’s function;\(^7\)
- review and assessment of the terms of reference, key outputs (including the main recommendations) of the central control units,\(^8\) including documentation and review of the current budget process;
- review of decentralized operations;
- review of application and general computer controls related to information technology;
- documentation and review of the current processes for identification, formulation, approval and implementation of policy revisions needed to reflect changes in IDA’s strategy, priorities, operational model, and identified risks; and
- integration of findings relating to effectiveness and efficiency from transaction-level work conducted under Part I, and particularly findings regarding inefficiency of current

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\(^6\) As explained in paragraph 5, this represents a revision from the formulation of this objective in management’s Part II Scoping Memorandum and aligns it more closely with the COSO standard for this objective.

\(^7\) Consistent with the Scoping Memorandum for Part II, management has conducted a review of the role of the Board of Executive Directors (the "Board"), its procedures, and decision-making tools. The results of this review are set out in management’s report on the role of the Board (included as the Attachment to Annex A of this report), which summarizes: (a) the primary control functions of the Board (consistent with its responsibilities under IDA’s Articles of Agreement, as interpreted through various decisions, legal opinions and other means); (b) the main tools, structures and other means for carrying out these functions (including a summary relating to the Board’s committees and their respective roles and functions, types of meetings and other means for deliberation and decision-making; types of Board documents and disclosure regime that applies to the main ones); (c) rules of conduct that apply to Executive Directors and their staff; and (d) more specific information regarding the function/role of the Audit Committee, which has the primary mandate for assisting the Board in overseeing IDA’s financial condition, risk management and assessment processes, the adequacy of governance and controls, and reporting and accounting policies and procedures. The Board under the auspices of COGAM is currently looking into broader internal governance issues relating to the role and operations of the Board. While management expects that this review would result in important findings and possible recommendations for improvement in various areas of Board operations, it does not expect the review to identify major gaps or weaknesses in the Board’s function. Management is therefore of the view that COGAM’s review is unlikely to have a material negative impact on management’s current assessment that the Board is functioning properly and is providing the appropriate governance and oversight of IDA’s operations.

\(^8\) See paragraph 42.
processes governing IL operations and work done under Part I to identify and review current processes and tools in place\(^9\) to monitor and report to senior management and the Board at various stages on progress of projects and programs supported by IDA toward achieving the agreed outcomes (both at the project level and at the country level).

### III. Management’s Assessment, Findings and Recommendations

14. This section sets out management’s overall assessment regarding the effectiveness of the current internal control framework over IDA’s operations, followed by more detailed findings of significant deficiencies identified by management and recommended actions to address them.

#### A. MANAGEMENT’S OVERALL ASSESSMENT

15. Under the COSO internal controls framework,\(^10\) Management is responsible for establishing and maintaining an effective internal control system. IDA’s management has assessed internal control over IDA’s operations, and based on this assessment, and reflecting the work undertaken by management, and attested to by the external auditor, during the FY07 ICFR process, management is of the view that the internal control system over IDA’s operations is adequate to provide reasonable assurance to Senior Management and the Executive Directors that:

- IDA’s published financial statements are being prepared reliably;
- IDA carries out its operations in compliance with the relevant provisions of its Articles of Agreement and operational policies and procedures, including the provisions relating to the use of funds for intended purposes; and,
- They are made aware, in a timely manner, of the extent to which IDA is moving toward effective and efficient use of its resources in meeting its operational objectives.

16. As part of its assessment, however, management has identified a number of significant deficiencies which require remedial actions—and effective monitoring of their implementation—in order to strengthen the internal control system over IDA’s operations. These significant deficiencies, described below, fall into five categories: (a) IL framework; (b) fraud and corruption; (c) PR and FM work, (d) identification of systemic risks; and (e) AAA and IT issues:

**(a) Issues relating to the current policy and procedural framework for IL:**

- Process inefficiencies, including a lack of focus on key risks and controls during preparation/design and supervision stages of IL projects.
- Outdated and complex policy framework for IL as reflected in multiple OPs and BPs that apply to IL operations.

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\(^9\) These include: progress reports on implementation IL and DPL operations (ISRs) and CAS progress reports, and project, DPL and CAS completion reports, as well as IEG evaluation of each ICR, CAS completion reports as well as country and thematic evaluations.

o Risk identification and reporting with an emphasis on information-sharing within the task teams and between staff and management during project supervision, including diffused accountability in such areas.

o Timely accessibility of operational documents primarily relating to IL operations.

(b) Issues relating to Controls for Managing Fraud and Corruption Risk in IDA-supported operations:

o Need for better design and integration of controls for managing fraud and corruption risks (reflecting, inter alia, lessons learned from precedents and INT work) into design/preparation and supervision/monitoring of IDA-supported.

(c) Issues relating to PR and FM

o Adequacy of controls in place to ensure consistent follow-up on PR issues by the task teams, including the need for better integration of PR staff in task teams and clarification of accountabilities for procurement issues and decisions

o Inconsistent implementation of PR post-reviews; and

o Inconsistency in quality arrangements for the documentation of FM supervision and some inconsistency in quality arrangements for oversight and monitoring of FM supervision.

(d) Issues relating to identification of systemic risks

o Inadequate mechanisms for risk aggregation and timeliness and consistency in monitoring, identifying (and formulating an appropriate response to) systemic risks.

(e) Other Issues:

o AAA processes and controls.

o Information Technology (IT) controls relating to password sharing in SAP, privileged access, and Infrastructure Change Management.

17. A summary of each of the above significant deficiencies identified by management together with recommended remedial actions are set out below.

B. FINDINGS AND RECOMMENDATIONS

1. Improving the IL framework

a. Rationalizing IL processes and strengthening controls

18. Transaction-level work conducted by management in Part I (including identification, mapping and testing of IL processes and controls), has identified significant inefficiencies in the current processes and controls that apply to IL, especially during preparation stages (from concept to approval). As reflected in management’s Part I report, IL is currently hampered by inefficient and often duplicative processes and reviews, often applied in a “one-size-fits-all” manner, irrespective of the level of risk, borrower capacity, track record, and similar factors. The absence of a risk-based approach to IL processes and controls undermines efficiency and effectiveness of these controls by over-regulating low risk projects while diverting resources and
management attention from addressing higher risk situations. Attention to proper risk identification and results monitoring during project supervision is diverted by excessive focus on preparation/appraisal stages. Such focus also contributes to increased project preparation/appraisal costs and delays in bringing projects to the Board for its consideration and approval.

19. **Recommended action.** In response to these and related findings of this assessment, management has launched a comprehensive effort to reform the investment lending instrument. An early concept for the proposed reform was shared informally with the Executive Directors in May 2007 through a technical briefing and a revised action plan has been prepared to reflect the results of this internal control review and reflect other developments, including the Middle Income Countries (MIC) and Fragile States strategies, the GAC strategy, findings of the Volcker Panel Report and the India DIR.\(^\text{11}\) A concept note on IL reform, which reflects the findings of this review, is scheduled to be discussed with the OVPs on October 20 and with the Board in January 2009. Integration of a risk-based model into the control framework governing IL is a key aspect of the rationalization of IL processes and controls. The principles of the new IL policy and the new risk-based control framework for IL are expected to:

- rationalize and prioritize key controls governing IL;
- facilitate appropriate differentiation of processes and requirements based on risk;
- set appropriate additional controls, resources, and reviews for higher risk operations/environments; and
- maximize efficiency and effectiveness of each control through rationalization and workflow automation
- strengthen risk identification and monitoring during supervision by, among other things, clarifying roles, responsibility and accountability between IDA and borrowers and within the institution.

20. Management expects to complete the first phase of IL reform, which will address the process and control issues during all stages (including more timely risk identification and reporting during supervision, clarification of roles, responsibilities and accountability within the task team, as well as better integration of fraud and corruption issues in project appraisal and supervision) in FY09-Q4.

**b. Reforming IL policies**

21. During Part I of the assessment, management identified that various OPs/BPs have not been keeping pace with the changes needed and/or introduced on the ground. As the main fiduciary policies (including OP/BP 12.00 related to disbursements and 10.02 related to FM) were issued in March 2007 and major instrument policies (including OP/BP 8.60 related to DPLs and OP/BP 8.00, related to emergency lending) are in place,\(^\text{12}\) this issue primarily affects OPs and BPs that apply to appraisal and supervision of IL. Consistent with the scoping memo


\(^12\) As noted in paragraph 39, work is underway to update OP/BP 11.00, Procurement.
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for Part II, management has assessed (a) how the proposed reform and consolidation of IL policies will help address this issue; and (b) how the current processes for policy revisions could be made more efficient so as to facilitate more timely updates of OPs and BPs.

22. Based on these assessments, management is of the view that the proposed reform of IL policies will address most of the outstanding policy updates issues. While this work is important from the Control Activities and Information and Communication points of view, the entity-level review conducted during Part II, including information from the ELC Questionnaires,\(^\text{13}\) confirmed that the current status of OPs and BPs does not have a material impact on compliance and operations objectives of IDA as a result of compensatory measures adopted to “fill in” the gaps created by the outdated OPs and BPs. These mitigating measures include issuance of Operational Memoranda and central and corporate guidance to staff. Based on management’s identification and mapping of the current process for policy revisions, management believes that the current backlog in OP/BP updates is due to the prescriptive and micro style and approach to OP/BP drafting and content rather than the process for introducing policy changes that require OP/BP revisions. The principles-based approach to preparation of new OPs and BPs reflected in the more recent policy reforms,\(^\text{14}\) which focuses the OP and BP statements on core principles and key controls rather than detailed rules and procedures characteristic of the older statements, should help minimize any future backlogs in OP/BP updates.

23. **Recommended action.** During Part I, IL was identified as the most over-regulated Bank instrument and is subject to approximately 30 of the Bank’s operational policies and procedures, many of which are misaligned with the current practice and evolution of the IL instrument. To address this shortcoming, which is the source of much inefficiency surrounding the current IL instrument, the IL reform effort will focus on consolidating and rationalizing the policies and procedures governing IL by creating a single principles-based “umbrella” policy for IL that would govern IL projects from preparation through completion. Reflecting lessons learned, including findings of this internal control review, the new IL policy would:

- replace the rigid “ring-fenced” IL project model with a flexible menu of design, funds flow and financing options to better meet development and funding needs of IDA’s varied clients;
- replace the current “one-size-fits-all” requirements with a risk-based approach to selection of IL design options and associated due diligence, processing, and monitoring requirements.
- reflect main principles governing redesigned IL instrument in a new principles-based umbrella policy governing IL from “identification” to exit.

24. Management expects to make a proposal for policy consolidation during the second phase of IL reform, following the completion of (a) Phase I that would address preparation/appraisal process inefficiencies and significant deficiencies in supervision as a matter of priority, and (b) broad consultations inside and outside the Bank to ensure that the

\(^{13}\) During the ELC Questionnaire process only OPCS identified OP/BP status as an issue.

\(^{14}\) These include: OP/BP 6.00 related to expenditure eligibility, OP/BP 10.02 related to financial management, OP/BP 12.00 related to disbursement, OP/BP 13.20 related to additional financing and OP/BP 8.00 related to rapid response to crises and emergencies.
new IL model meets and reflects the needs and expectations of the Bank’s clients, partners and shareholders. This second and final stage of IL reform is expected to be completed in FY10-Q4.

c. Risk identification and reporting and better information sharing

25. Management’s assessment of entity-level controls has found an issue with timeliness and scope in reporting of risks generally, and in the context of project supervision in particular. Sources for this finding include management’s assessment of responses to the ICFR and ELC Questionnaires, a review of the Risk and Opportunity Workshop (ROW) results, and findings reflected in recent outputs/reports of several central control units, including IAD, QAG and IEG. Given that timely and accurate reporting on risks and project implementation issues is essential to ensure that appropriate and timely decisions and actions are taken to address risks and improve outcomes, this issue merits prompt management attention to formulate and implement an effective remedial action.

26. **Recommended action.** This finding has pointed to the need to strengthen incentives, including: (a) staff incentives and accountability; (b) management tools and accountability; and, (c) resource reallocation mechanisms. These will promote open and timely identification and reporting of risks. Some management actions are already underway to improve candor and realism in implementation supervision reporting in response, at least in part, to IAD’s, QAG’s and IEG’s findings. These include:

- a cross-regional review of ISRs by OPCRX was conducted as input into the Focus on Results—“IDA 14 Results Measurement System and Directions for IDA 15.”
- preparation and dissemination of important reference documents, including the launching of an e-learning module in FY08 Q4 to assist teams in preparing and updating ISRs;
- regular reviews of ISRs by the regions, with guidance from OPCRX, including a guidance on Maintaining a Results Focus in ISRs; and
- preparation by each Region of specific guidance for ISR reviews to ensure adequate baselines, and to review quality and realism.

27. In addition, as part of IL reform management also expects to introduce measures that would improve timeliness and accuracy of risk identification and information sharing within the task team and between management and staff, including such measures as (i) mechanisms for reallocation of resources to address newly-identified risks; and (ii) incentives and management actions to encourage accurate and timely reporting of risks and issues in operations, including project performance.

d. Incentives and instruments to foster accountability and compliance

28. Management’s assessment of entity-level controls has identified that accountability, compliance and internal control responsibilities are not adequately reflected in performance.

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15 For example, the OPCS Results Agenda Website includes a Quick Reference Guide on Results in Operations; the IDA RMS Fact Sheet; Maintaining a Results Focus in ISRs; Baselines in ISRs; and Results and Harmonization in Bank Operations (including supervision). In addition, the results terminology is periodically updated and posted on the Website.
management tools such as OPEs or promotion criteria. Nor does there seem to be a strong link between performance evaluations and individual accountability: for example, job descriptions and performance evaluations do not usually contain specific references to internal control related duties, responsibilities, and accountability. Concerns about the adequacy of current incentives to promote accountability, compliance and quality were also reflected in several units’ responses to the ELC and ICFR questionnaires. Several responders expressed a concern that individual staff and units are primarily rewarded for specific results such as project delivery to the Board and project disbursements and completion, with less attention being paid to the method or quality of these achievements. Potential issues with accountability arrangements were also reflected in the Volcker Panel Report (referenced in footnote 15) and the India DIR (referenced in footnote 10).

29. Some of these concerns are being addressed by ongoing activities in the accountability and ethics areas, such as emphasis on ethics and controls in the orientation program provided for all new Bank hires and implementation of appropriate disciplinary action in response to departures from approved policies and procedures or violations of the code of conduct pursuant to Staff Rule 8.01. In June 2008 the Bank has issued a strengthened, dedicated whistle-blowing policy and amended the Principles of Staff Employment to enhance its current handling of whistle-blowing reports and claims of whistle-blowing retaliation. The new policy, principle and staff rule puts the Bank Group at the leading edge of whistle-blowing protections amongst international organizations, consistent with the highest standards of good governance and the on-going efforts of the Bank to safeguard its integrity and effectiveness.

30. Management has long-recognized the challenge of managing performance in the Bank— which is key for promoting individual and professional accountability. This has been emphasized most recently in the Report of the Performance Management Working Group published in July 2007. Prompted by the Report, HRS launched HR Insight, a new website dedicated to sharing HR-related data, information and research with Bank Group staff. Efforts have also been made to exercise more differentiation in the recent SRI awards, to ensure that high performers are rewarded.

31. **Recommended action.** Given the importance of individual and professional accountability to the effectiveness and efficiency of an internal control system, senior management is undertaking a corporate review of responsibilities, accountabilities and quality oversight. This review will include several components, including (i) existing oversight and quality assurance arrangements to identify shortfalls in quality, including the roles and methodologies of the institutional mechanisms such as QAG, IEG, Regional Quality teams, (ii) the existing quality and accountability arrangements for operations, including roles and responsibilities within the task team and processes and controls in place to ensure proper oversight, (iii) development by HRS of a comprehensive roadmap/strategy for enhancing performance based on the diagnosis of the root causes of dissatisfaction with current performance management, developed by the Performance Management Working Group, and (iv) continuation of HRS efforts to enhance the HR Insight website to increase further the transparency of HR-related data. Components of this work will be reflected in: the QAG review, expected to be completed by January 15, the first phase of IL, expected to be completed in FY09-Q4, including in particular the integration and clarification of responsibilities within the task team and strengthening of the supervision model.
e. Timely accessibility of operational documents

32. During “compliance testing” conducted by management in Part I, management identified a problem with accessibility of operational documents. The documents requested by management to support the processes and controls identified were not easily accessible. Although after an extensive effort management was able to obtain 93% of the documents requested, this exercise identified the need to strengthen document retention practices and improve accessibility of operational documents. During Part II management confirmed that this issue is indeed linked to both, the Control Environment and Information and Communication components of COSO at the entity level, as was suggested by IEG in its Part IB report. Consistent with IEG’s preliminary recommendation, the review conducted by management also concluded that improved IT systems to support IDA’s operations would have to be an integral part of the solution to these issues.

33. **Recommended action.** Management has already begun to address the document retention and accessibility issue by setting up a Task Force in FY07 to look at retention, filing and accessibility of operational documents and come up with recommendations for improvement. Working closely with ISG, the Task Force has made a proposal for addressing the issues identified through automation of key controls for IDA’s primary operational tools (CAS, DPL, IL) into the Bank’s documentation system. Under the proposal, this work would commence with automation and integration of IL processes and controls, where most issues with documents accessibility occurred. The work on the automation system will proceed in close coordination with the first phase of IL reform and will be part of the Operations and Knowledge Management Systems Program (OKSP, previously known as the Enterprise Content Data Management (ECDM)). The new system for IL will be piloted in FY09 and is expected to be fully in place by the end of FY10, in close coordination, and forming a part of, the roll-out of IL reform.

2. Better integration of controls for managing fraud and corruption risks into design and supervision of Bank-supported operations

34. IDA’s anti-fraud and corruption strategy can be divided into three phases: Phase I, which focused on setting out the intellectual case that good governance and an attack on corruption must be key parts of efforts to sustain economic growth and alleviate poverty, Phase II, which focused on formulating an appropriate anti-corruption strategy and its adoption by Senior Management and the Board; and Phase III, which focuses on the implementation of the anti-corruption strategy through its integration into the Bank Group’s (including IDA’s) daily operations. Having been the leader in making an intellectual case against corruption (as noted in the Volcker Panel Report discussed below), and having demonstrated the depth and

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breadth of the management and Board commitment to this agenda through the adoption of the GAC strategy,\textsuperscript{17} IDA has actively moved into Phase III of this work.

35. Phase III builds on and reflects: (i) the firm commitment and actions of IDA’s senior management, starting with the President, to make its fight against fraud and corruption a core element of IDA’s operations; (ii) diagnostic and assessment work performed or commissioned by management to identify areas where the controls for managing F&C risks need to be strengthened; (iii) ongoing efforts and experience with strengthening country client institutions and systems that are essential for effective and efficient management and utilization of public resources, including safeguarding these resources from fraud and corruption; and (iv) roll-out and implementation of specific actions to strengthen controls and improve effectiveness of IDA’s efforts in managing F&C risks that reflect the work and recommendations flowing from the work under items (i)-(iii). As summarized in the Attachment to this report, much progress has been achieved in this area particularly over the past 6-12 months, putting the Bank well ahead of other institutions dealing with these complex and challenging issues. Management is committed to deepen and broaden these efforts to: (i) continue building and strengthening mechanisms to monitor and manage F&C risks in IDA-supported operations, including expanded Bank-wide staff (and particularly TTL) training, and (ii) refine and improve F&C controls as more knowledge is gained about the weaknesses that still exist (which needs to be a continuous effort to reflect on lessons learned and a growing body of experience).

36. \textit{Recommended action.} While the efforts described above have strengthened IDA’s controls for identifying and effectively managing F&C risks in operations, more needs to be done to “expand staff skills and broaden behavioral change in order to deepen, systematize and mainstream good practices across all of the Bank Group’s work.”\textsuperscript{18} To this end, management is committed to implementing additional corrective actions outlined below:

37. Clarifying responsibilities and accountabilities for addressing fraud and corruption through:

- Adoption of the new INT strategy (expected to be discussed with the Audit Committee in early calendar 2009).
- Establishing appropriate protocols of cooperation between INT and the Regions on handling allegations of F&C.
- Reform of processing and supervision of IL operations as part of Phase I of IL reform, expected to be completed by FY09-Q4;
- Expanding staff skills and broadening behavioral change in order to deepen, systematize and mainstream good practices across all of the Bank Group’s work by introducing improved tools (including training) and processes for identifying and managing F&C risks through:
  - Developing and mainstreaming improved tools for managing F&C risks in project design and supervision stages through the work being carried out by the GAC in Projects Working Group, supported by OPCS, which is undertaking a substantial

\textsuperscript{17} Implementation Plan for Strengthening the World Bank Group Engagement on Governance and Anti-Corruption, OPCS September 28, 2007 (the GAC Implementation Plan).

\textsuperscript{18} The Volcker Panel Report, page 2.
work program aimed at improving quality and consistency in approaches to fraud and corruption risk mitigation at the project level. The main elements of this work, that are well underway, include:

- GAC Audit and Assurance Toolkit, launched by OPCFM, which is designed to help task teams enhance the effectiveness of financial audit and provide guidance on other types of audit and assurance engagements that focus on fraud and corruption risks, such as technical and contract audit.
- The updates under preparation to the FM Practices Manual which will incorporate guidance on fraud and corruption.
- Preparation of guidance for FMSs by OPCFM on how to better identify and manage corruption risks through smart project design (to be supported by web-based knowledge sharing tools).
- To support the mainstreaming of the GAC agenda at the sector and project levels, preparation of an OPCS paper on GAC good practices at the project level “Dealing with Governance and Corruption Risks in Project Lending: Emerging Good Practices” (draft completed and circulated for comment). The paper would: (a) provide Task Teams with a common conceptual framework for understanding GAC issues; (b) highlight some of the key lessons learned over the past several years and provides examples of emerging good practices at the sector and project level; and (c) indicate areas where further work is required in order to fully support Task Teams in this relatively new area of emphasis. The final paper is expected to be issued by the end of Q3 FY09.
- A Training Program for Task Teams is being developed, with two pilots already conducted, and plans to roll this out in FY 2010. The curriculum covers the 4 major components of the GAC agenda: (a) the CGAC initiative at the country level; (b) assessing governance and corruption risks at the sector and project level; (c) mitigating project risks through “Smart Project Design” and the development of project-specific Anti-Corruption Action Plans; and (d) the supervision of high corruption risk projects.
- An initial stock-taking of AAA and investment lending operations with significant GAC components has been completed, and is being converted to a searchable database that can be accessed by Task Teams to provide examples of innovative approaches to risk assessment and risk mitigation.
- Work is underway on “case studies and good practice notes” that illustrate and elaborate on the tools and approaches (see below) that are being developed to improve governance and reduce corruption at the sector and project level. These will be disseminated through an on-going program of brown bag lunches. They will also be available as a publications series and on the new GAC in Projects web portal.
- A GAC in Projects Peer Learning Network has been established, with a rapidly growing “community of practitioners” that will be supported by the interactive web portal noted above. Practice Leaders are also being identified at the regional and sector level, and several units have established either full-time focal points (EAP and SAR) or “on demand” Advisory Units (ECA and INF).
Building on the progress achieved in developing and testing “smart” project design and more effective and more appropriately resourced project supervision, which reflect lessons learned, including systemic issues drawn from INT investigations and DIRs and create a more effective risk management framework to help prevent, deter, detect and address fraud and corruption, which are to be reflected in the new approaches to project design/appraisal and supervision to be developed as part of IL reform.

- Reviewing staff incentives (performance reviews, promotions, rewards, and visibility) to ensure that they are aligned with the anti-corruption agenda through discussions at an MD-chaired GAC Governance Council (ongoing).
- Preparing and monitoring (with OPCS support) specific action plans for following up on INT reports (a small team for the follow-up on post-INT report action plans is proposed to be established in OPCS with effect from FY2009 and a new position has been advertised by OPCS).
- At the entity-level, specifically including F&C risk among the risks facing the institution in the new Annual Integrated Risk Report, mentioned in paragraphs 43 and 45 below, which will replace the current Risk Scan tool.
- Specific actions in the procurement area to address fraud and corruption (reflected in paragraph 39 below).


38. **Procurement.** During Part II management assessed quality arrangements over PR work relating to project appraisal and supervision and has identified the need to strengthen quality arrangements, business processes and adequacy of documentation relating to PR during project preparation/appraisal and supervision stages. This review found that (a) quality assurance arrangements for procurement are in place and are generally sound and (b) the regional variances identified are in line with the high degree of decentralization and broad mandate of the Regional Procurement Managers (RPMs). However, management’s review also identified two issues that need to be addressed: (a) adequacy of controls in place to ensure consistent follow-up on PR issues by the task teams, including the need for better integration of PR staff in task teams and clarification of accountabilities for procurement issues and decisions; and (b) consistency in implementation of post-reviews. In management’s view, these issues, combined with the findings of Part I of this exercise, rise to a level of a significant deficiency in PR area, which requires implementation of monitorable corrective actions. Several corrective actions recommended by management in response to deficiencies indentified under Part I of this review have already been implemented. These include:

39. **Recommended action.** To address the issues identified, management recommended a plan of corrective actions, some of which have been implemented already, while others are underway.

**Actions in place:**

- Improving controls and quality of complaints data base:
o Starting in FY07, the procurement complaints database has been made a key control and management tool, and enhancements to the database include automatic alerts to remind RPMs of pending cases, to seek RPM clearance when closing cases, and to track complaints related to late payments. OPCPR monitoring of complaint follow-up has been strengthened.

- Strengthening PR/INT cooperation on management of F&C risks:
  o In July 2008 a Memorandum of Understanding was signed between OPCPR and INT on the prevention of Fraud and Corruption in Procurement.
  o In December 2008 a joint INT/OPCPR guidance note on identification and handling of red flags during the project cycle was issued.

**Actions underway:**

- Full Integration of PR staff and tasks in project teams:
  o Develop mechanisms for early and full integration of PR staff in the project teams and of PR tasks during the project cycle
  o Clarify the sharing of responsibility for key PR decisions at preparation and implementation stages between TTL and PR staff and Sector Manager and RPM, including mechanisms to resolve disagreements and raise awareness of TTLs/sector managers
  o Enhance a Procurement Certification system that would increase awareness and importance given to procurement work
  o Develop guidance and criteria for assigning PR ratings for the ISR, and mandatory recording of revisions to such rating by sector staff.

- Updating procurement policy and procedures:
  o Update of OP/BP 11.00, *Procurement*, is being finalized to incorporate, *inter alia*, risk management and fraud and corruption issues, and to document the already enhanced complaints handling (expected to be issued in January 2009)

- Bank-wide roll out of PR risk assessment tool:
  o Finalize a PR Risk Model/Risk Management Tool that specifically focuses on F&C issues is for piloting in the spring of 2009. (It will be used under the country systems pilot first and will be made mandatory for Bank-wide use later in 2009.)
  o Revise templates for the PAD Procurement Annex in light of new initiatives, including risk-based procurement assessments that include a focus on fraud and corruption and to reflect the work on risk-based approach to processing of IL operations as part of the first phase of IL reform (to be completed by June 2009)

- Strengthening OPCPR/PSB Roles:
  o Review, by March 2009, the roles of the Procurement Sector Board (PSB) and OPCPR with a view of: (a) expanding it to identify areas that may merit harmonization of
regional practices; (b) strengthening the advisory role of the PSB to respond to the Regions’ needs; and (c) monitoring regional fiduciary compliance and quality, including post review.

40.  **Financial Management.** In FM, Management found that while Quality Assurance (QA) arrangements have been put in place to oversee FM arrangements for the use of IDA financing, the quality and documentation of regional QA arrangements is inconsistent and does not fully comply with the FM Practices Manual (FMPM), particularly during project implementation. Variations in Regional QA exist, and while many of these make sense, there is a need to ensure consistency in the quality of FM work, as defined in the FMPM. Management’s assessment identified issues in three areas: (a) Documentation of review of audited financial statements by an FM specialist and management oversight of Audit Report Compliance Systems (ARCS) data—in some Regions, it was not possible to verify regular FMS review of audit reports because ARCS data entry was considerably out of date; (b) Documentation of FM supervision—there are inconsistent quality arrangements for the documentation of FM supervision work, including supervision planning, supervision reporting, and follow-up on FM action items. Quality arrangements to support the filing of FM documents are also inconsistent, making it difficult to validate that FM work has been undertaken; (c) Timing of quality interventions during supervision and identification and monitoring of risky projects—there are inconsistencies and gaps in quality arrangements for Regional FM managers’ oversight and monitoring of FM work during project supervision. In some Regions, there is no systematic monitoring of interim financial reports. This could result in FM issues not being identified and corrective actions not being taken on a timely basis.

41.  **Recommended action.** The FM Sector Board already has actions underway to strengthen quality arrangements, including:

- Completion of Phase I of the Joint CSR/OPCS Evaluation process (Phase II will be launched in January 2009).
- Adoption of the RAPMAN/PRIMA system by all regions.
- Centralized monitoring of the ARCS audit tracking system by OPCFM and a rapid reduction in the number of outstanding audit reports.
- The FM Sector Board also took the following actions to strengthen specific F&C controls in the FM area:
  - Issuance in June 2007, of an FM Approach Paper to GAC,19
  - Establishment of an FM GAC Working Group to support the development of good practices, guidance and training for FM staff
  - Issuance of an Audit and Assurance Toolkit
  - Draft FM Guidance on dealing with fraud and corruption in project design has been circulated to the FM Sector Board.
  - Work is underway to develop similar guidance on enhanced project supervision and FM "red flags", supported by web-based tools and guidance, including a database of projects featuring FM anti-corruption features.

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Training on GAC was provided to all FM staff at the 2008 Fiduciary Forum and further training is envisaged.

- Additional actions that are underway to address deficiencies identified in the FM area include:
  - Review and update of the FM Practices Manual, which serves as the main operational guide for FM staff, with the revised FMPM expected to be issued in June 2009. (Findings of this review will be incorporated into the final methodology for the Joint Evaluation).
  - Regions have consolidated and updated their QA arrangements (including QA-related information on their websites), and will introduce further updates as necessary, including to align these arrangements with the issuance of an updated FMPM next June 2009.
  - Considerable progress has been achieved in most regions in updating the ARCS for all actions related to audits that were due in FY05 through FY07 and in clearing backlogs relating to earlier years. In addition, Regions have largely completed entry of baseline data on interim financial reports into PRIMA by October 31, 2008.
  - Pending the establishment of the institutional Enterprise Content and Document Management system, the FMSB will develop and communicate good practices and additional guidance to staff by December 31, 2008.

4. Risk aggregation

42. Management has identified that while important review and evaluation work is being carried out throughout the institution by the central control units (including IAD, IEG, INT, QAG, CSR, and the Inspection Panel), risk and control activities remain fragmented, resulting in duplication of effort and potential gaps in risk coverage. IDA also currently lacks a consistent mechanism for aggregating and prioritizing the results of this work. This finding is based on management’s review of the terms of reference, key outputs (including recommendations) of the central control units, assessment of responses to the ELC Questionnaire, and relevant observations set out in the Volcker Panel Report and the India Detailed Implementation Review (DIR).

43. **Recommended action.** This finding merits strengthening of the existing management tools for integrated risk management. To this end, management (through CSR) intends to move toward an annual Integrated Risk Report intended to (a) describe overall risks facing the institution, (b) identify units responsible for management and oversight of risks identified, and (c) assess potential gaps and overlaps, and (d) develop a dashboard of risk findings from the various assessment activities, and (e) over time, assess the quality and consistency of the processes in place.

44. In addition, a more in-depth review of the central control units may be merited, including complementarities in their respective methodologies, terms of reference, outputs and current mechanisms for information-sharing and consolidation of their respective findings and recommendations. In management’s view, such review should:

- Identify ways to rationalize and improve effectiveness and efficiency of checks and balances provided by the central control units,
• explore various mechanisms for better risk aggregation and assessment/review rationalization, including mechanisms in place to validate and prioritize key risks for monitoring and testing as well as defining opportunities for improvements to controls and management activities.
• assess mechanisms for linking systemic risks identified from time to time with objectives, initiatives, and business processes, opportunities for alignment and coordination across the institution.

45. The Integrated Risk Report is expected to be completed by FY10. Management is also currently conducting a review of QAG, but believes that a broader review described above would also be merited. The review is expected to be completed by January 15, 2009. Management would welcome the views and guidance of the Audit Committee relating to such broader review.

5. Other significant deficiencies
   a. AAA processes and compliance

46. As mentioned in the Scoping Memo for Part II, and following the request of IEG and the Audit Committee to include AAA within the scope of this exercise, during Part II, Management (a) identified and mapped current processes that apply to the main AAA product line, Economic and Sector Work (ESW) reports, (b) conducted a walkthrough of the mapped processes, and (c) tested compliance with such controls using a sample of randomly selected ESW reports completed and delivered to clients during FY07, in a process similar to that performed for IL, DPL, and CAS product lines during Part I. The focus on ESW (and for sampling purposes, on ESW reports) was in large part due to the fact that ESW funding has traditionally absorbed the major share of AAA funds and ESW reports account for over 80% of total ESW spending.20 The process mapping exercise will inform management’s larger-scale review of AAA covering both IBRD and IDA, currently underway.

47. In ESW Reports randomly selected for compliance testing, non-compliance with controls was identified in 25% of control steps involved in the ESW process. It should be noted, however, that roughly half of the instances of non-compliance were due to mismatches between dates recorded in SAP and the actual dates of application of such controls (e.g. the dates of the Concept Review meetings of some of the transactions differed from the dates for such meetings recorded in SAP).

48. Recommended action. Management is undertaking a broad review of the processes and controls, including systems and monitoring, that apply to AAA in order to simplify and strengthen them where needed, and ensure they are updated to take into account the wide variety of AAA currently carried out by the Bank. This review will also address the compliance weaknesses observed, along with other issues that have been raised by IEG and QAG in recent

20 The sample was drawn from the universe of ESW Reports completed as of September 16, 2007, and whose cost exceeded $100,000. These types of ESW Reports accounted for 90% of ESW Reports completed. ESW as a whole has consumed approximately 67% of the AAA budget.
related reviews of AAA. Management expects to complete this review and discuss the recommended changes with CODE in FY10.

**b. IT-related issues identified as part of the ICFR exercise**

49. During the ICFR review three significant deficiencies were identified in connections with IT-related issues. The first related to password policy breaches in SAP, as identified by IAD in its FY07 “Identify and Access Management” audit. The audit identified that SAP passwords are widely shared by Bank staff which may have resulted in some unauthorized expenses in the financial statements. The second related to the scope of privileged access and monitoring of activities in privileged accounts which were deemed to need rationalization and strengthening to limit risks of misuse. The third related to change management controls associated with Infrastructure Change Management and the need to ensure consistency of application of these controls.

50. **Recommended action.** In response to these findings, Management has recommended and as part of the ICFR program is carrying out corrective actions to (a) address the password sharing issue, (b) strengthen controls around Information Security to rationalize and further limit privileged access to system applications and monitor changes made by IT staff using such privileged accounts; and (c) strengthen controls around Infrastructure Change Management to ensure that change management controls are applied consistently and exceptions are reviewed and authorized by appropriate authority.

**C. Monitoring Arrangements**

51. Management intends to implement the above remedial actions over the next 18-24 months and report to Senior Management and the Executive Directors on the progress of their implementation and results achieved. OPCS and CSR will take the primary responsibility for such periodic monitoring and reporting, with the first progress report to be prepared and discussed with the Executive Directors in the early fall of 2009, in time for the IDA 15 mid-term review.
Attachment to Management’s Report
Fraud and Corruption: Summary of Actions Implemented

1. **High-level commitment and actions.** As the President stated in his recent address to staff during the Integrity Day on December 3, 2008, the Bank’s commitment to integrity is at the core of all it does. The Bank, at its highest levels, is not just making the case but is actively implementing the anti-corruption agenda, as evidenced by: (i) the swift actions it has taken and specific measures it has put in place over the past 11 months in response to the Volcker Panel Report (discussed below), (ii) senior management hands-on approach and involvement in decisions relating to delays or suspension of operations affected by fraud and corruption issues; (iii) detailed and candid coverage of fraud and corruption risks in Bank documents, including CASs, project documents, and periodic updates by management to the Board on specific actions and progress achieved in this area (as well as remaining challenges).

2. **Diagnostic work.** The Volcker Panel, India DIR, and this IDA internal controls exercise have all served as key diagnostic tools to assess the status of controls over management of F&C risks in operations and recommend areas for improvement. To maximize effectiveness of its implementation efforts, including identification of areas for improvement, in February 2007, the World Bank President, in consultation with the Board, requested an independent panel of experts (the Volcker Panel) to review the operations of INT, the Bank’s central control unit responsible for, among other things, investigating allegations of fraud and corruption in operations financed by IDA and other members of the World Bank Group. The findings and recommendations of the Volcker Panel, as set out in the Volcker Panel Report issued in September 2007, identified that much remained to be done in mainstreaming fraud and corruption issues into IDA’s daily operations and has included 18 specific recommendations to help with this effort. Additional concerns about the effectiveness and robustness of controls over fraud and corruption in Bank-supported operations also were raised in INT’s Report on the Detailed Implementation Review of the India Health Sector (the “India DIR Report” ) , issued by INT in December 2007. The issues identified in these reports were consistent with management’s findings resulting from its assessment of entity and transaction level controls. Key among these were findings relating to the need to: (i) better integrate INT and the results of its work into IDA’s operations in order to improve management of F&C risks that may arise in the context of IDA-funded projects; (ii) specifically embed fraud and corruption risk assessment in many of the existing risk assessment processes; (iii) undertake assessment of F&C risks in a specific and systematic way throughout the institution; (iv) address more consistently as part of program and project design at a portfolio and project level, the vulnerabilities to fraud and corruption in countries with systemic corruption; (v) focus on incentives that would lead to consistent monitoring, reporting, and timely response to, implementation risks generally, and fraud and corruption issues in particular during project supervision; and (vi) develop new and/or improve existing tools and methodologies in all areas (project design, supervision and evaluation) using lessons learned, including the work of INT, in order to ensure appropriate flagging and treatment of fraud and corruption issues.

3. **Experience and tools for country-level work.** IDA has much experience with conducting country-level ESW work that helps assess and identify systemic issues that could undermine the country’s development efforts due to weaknesses in the country’s systems, institutions, and

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21 See the Volcker Panel Report, footnote 16 to this Report.
internal controls frameworks responsible for management and utilization of public funds. Such work is reflected in fiduciary ESW (in particular CPARs and/or joint fiduciary assessments i.e. combined CPAR/CFAAs which have become the quasi norm in the last 4/5 years), which provide the basis for assessing country systems and defining mitigation measures in DPLs and PRSCs as well as assess fiduciary risks at the country level that is an important input into CAOs. In addition, many projects that address public sector management have included PR and FM components, several grants (e.g. IDF) have focused on fiduciary strengthening, and close coordination with other donors as part of the harmonization efforts has helped address the capacity-building issues especially in fiduciary areas. This is monitored by the number of completed CPARs and the various Bank initiatives. In addition, much work is being done to strengthen country systems under the country system pilot in the procurement area, which focuses on assessing, strengthening and building on country’s procurement systems. It is also important to acknowledge the efforts in the FM area both as part of increasing number of projects that can rely on country’s own FM systems and as a key focus of actions that underlie assessments and strengthening measures addressed in an increasing number of DPLs and PRSCs. Strengthening and building country systems in these key areas has been and increasingly is an important focus of the Bank’s institution-building, governance and fiduciary support work in its client countries. Indeed, over 50% of DPLs in FY07 (up from an average of 24% in 1990-94) included conditionality on public sector governance, including in the areas of procurement, financial management, and budget transparency. While it is not a new area of emphasis, the importance of this work under the GAC strategy, combined with the work underway to implement the recently approved country systems pilot in procurement area, provide an added emphasis to the Bank’s efforts to strengthen the effectiveness, efficiency, reliability and transparency of control systems and institutions in client countries with the help of all of Bank’s existing tools and instruments. In addition, Bank FM Policies permit the use of country systems when these are assessed as being appropriate i.e. the challenge for the FM Sector is to accelerate the use of country systems when circumstances permit (presently estimated at 62% of disbursements - Monitoring Survey 2008, Paris Declaration). The 2007 FM Sector Approach to Governance and Anti-corruption identified country systems as one of the key areas of focus for FM work, identifying in particular the need to strengthen key institutions of accountability, including government internal audit functions, supreme audit institutions and legislative oversight committees. The Bank’s engagement with these institutions has been stepped-up. For example, a Global Partnership Agreement between the International Organization of Supreme Audit Institutions (INTOSAI) and Donors is under preparation. Guidance is also being prepared to help FM staff in assessing the adequacy of country FM systems for use in Bank supported operations. Moreover, the ongoing PEFA Program, Phase III of which was agreed with the EU, IMF and other bilaterals in June 2008, enhances IDA’s ability to strengthen country systems through the use of a common results measurement framework and joint fiduciary diagnostic work (including with PREM and Procurement).

4. **Management actions to strengthen controls for managing F&C risks at country and project level.** Over the past 12 months, management has undertaken proactive and concrete actions in response to findings and recommendations made in the context of the primary diagnostic tools, and particularly the Volcker Panel Report, India DIR and this IDA internal controls assessment. Much work has been done at the country level as well as part of management’s implementation of the GAC strategy. As reported in the recent GAC progress report on implementation of actions in response to the India DIR, discussed with the Board in
October 2008\(^\text{22}\), the overlap between the issues raised in the context of the India DIR, management’s actions designed in response to the Volcker Panel Report, and the findings of this IDA internal controls assessment, has greatly contributed to management’s ability to define a concrete plan of systemic Bank-wide actions for heightening the Bank’s effectiveness in the governance and anti-corruption area, including specific tools for addressing the relevant issues. These include specific actions in the following key areas:

- **Dissemination of lessons learned**, through (i) distillation of lessons learned from INT work by its Preventive Services Unit (PSU), designed as a tool which could be used for didactic purposes throughout the institution; (ii) at least 30 discussions and learning events carried out throughout the Bank by OPCS, SAR, and INT to disseminate lessons learned from India DIR; and (iii) training seminars carried out by the PSU and its collaboration with specific project teams to help them define their governance, accountability and anti-corruption plans at the project level.

- **Strengthening project supervision** through compilation and dissemination via the “GAC in Projects” network of good practice in such areas as 3rd party supervision and “smart” supervision.

- **Specific measures in procurement area:**
  - Development and roll-out of PR Risk Model/Risk Management Tool that specifically focuses on F&C issues, to be piloted in the spring of 2009. It will be used under the country systems pilot first and will be made mandatory for Bank-wide use later this year. The F&C module of the risk-management tool that will become part of the system in the spring of 2009 draws from the red flags identified by INT and the regions.
  - Deepening of the cooperation between the Procurement Anchor in OPCS and INT: A Memorandum of Understanding between OPCPR and INT on the prevention of Fraud and Corruption in Procurement was signed by VP OPCS and VP INT on July 28, 2008. It presents a framework to facilitate a joint approach in preventing F&C and lays down the areas of cooperation between INT and OPCPR. In addition, a joint work program relating to preventing F&C was agreed to by both units. (Due to confidentiality of information in the INT databases, it was agreed that OPCPR will not have access to the INT data base, but INT will be given access to OPCPRs complaints database on an as need basis.)
  - As described in paragraph 8 below, much work has been done to improve the completeness, operation and usage of the complaints data base which is an important source for identifying potential F&C issues.
  - OP/BP 11.00 has been revised and discussed extensively at the Procurement Sector Board; it is expected to be issued by the end of January 2009. OPCPR is also conducting an overall review of the guidance and other tools/ information on its website including all the guidance notes issued and will update them as necessary and at a minimum to be in line with OP/BP 11.00.

\(^{22}\text{Strengthening the World Bank Group Engagement on Governance and Anti-Corruption, October 21, 2008 (the GAC Progress Report)}\)
Specific tools for addressing fraud and corruption at project level, have included: (i) the development of GAC in project guidelines by “GAC in Projects” team under the GAC Implementation Plan (these have been discussed with teams across the Bank and are being finalized for issuance this month); (ii) lessons learned and best practices on GAC in projects are available (and being constantly updated and posted) on the GAC in Projects” website, supplemented by peer learning and other training events in this area across the Bank.

Strengthening financial audits through development of standard terms of reference to widen financial audits to cover performance issues and procurement. These have been issued in draft form and will be available in December for task teams interested in pursuing this more detailed type of audit. These new approaches will be disseminated via the Financial Management Sector Board.

In the health specific area, an assessment of Bank procurement procedures for pharmaceuticals is now complete and internal discussions are underway. A component of the recent HD week (fall 2008) was dedicated to “Governance and Accountability: Issues, Diagnostics, and Implementation Tools for Health”.

Strengthening accountability: The Bank is also taking action to re-enforce the accountability of managers on all sides of the matrix with respect to their respective areas of responsibility.

Specific actions in response to the Volcker Panel Report. Management also took swift and proactive actions in response to the recommendations in the Volcker Panel Report (Management’s Response is referenced in footnote 15 to this Report), with actions already implemented on 16 of the 18 recommendations (with the remaining two well underway). These actions have gone a long way to transforming INT from a segregated and rather insular function to a core part of the Bank in its fight against corruption. INT has rapidly moved toward the core of operations, without, however, losing its independence as one of the central control units that forms an essential part of the Bank’s internal control system. Key among these transformative actions are:

- elevation of the INT head to a VP level
- the establishment of a PSU within INT, which has as its major role the dissemination of the results of INT’s investigative work, and collaboration with operations to build these lessons into project design
- revision of INT’s disclosure policy relating to its work, thus making its findings and lessons that can be drawn from it much more accessible;
- the establishment of a very close relationship and partnership between INT and the operational complex through, in part, its close partnership with OPCS and the regions;
- inclusion of INT in Bank-wide senior management dialogue and reviews through INT participation in Operations Committee reviews and OVP meetings
- INT assistance to task teams that seek its advice, and increased training and learning on fraud and corruption issues carried out across the Bank in close partnership between INT, OPCS, PREM, and the regions
- the establishment of the Independent Advisory Board which is an important tool for confirming and building confidence relating to fairness and effectiveness of INT work.
6. The new INT strategy, to be discussed with the Audit Committee in January 2009, also emphasizes this transformation and charts a road ahead to maintaining and deepening the role of INT as a core part of the Bank while maintaining its independence.

7. **Actions and examples of country-level and project work.** As management also reported in its GAC Implementation Progress Report, discussed with the Board in October 2008 (see footnote 2), much work has been done to mainstream the GAC agenda at the country level. Specifically, 27 countries are now participating in the CGAC program, which allocated specific additional resources of $100,000 per participating country to identify, deepen, systematize and mainstream engagement on governance and anti-corruption at the country level. The CGAC initiative has resulted in development and refinement of systemic diagnostics of governance challenges and reflection of these issues in CAS for several countries. As indicated in Table 1 of the GAC Progress Report, GAC issues were adequately integrated in 64% of CASs discussed with the Board in FY 2007/08, with 32% (a jump from 19% compared to CASs discussed in FY 2006) of the CASs rated “high” in terms of providing a diagnosis of governance conditions and corruption risks. Indeed, engagement on governance and anti-corruption issues has increasingly become a part of the process for CAS design and preparation and its content. In countries where corruption issues have surfaced in the context of Bank projects, there have been serious and concerted responses at the CAS level. Examples include the CAS update in Kenya, following the DIR for health and education, and the recent Indonesia CAS which has GAC as its centerpiece. Recent examples of CASs that specifically address GAC issues also include the India CAS and the Zambia CAS, which are particularly striking in the candor and depth in how these key issues are addressed. In many other countries which have not yet gone through the C-GAC process, GAC issues also feature prominently in the CAS. In addition, issues of governance and fraud and corruption are increasingly permeating project design and are reflected frankly and comprehensively in project documents, including in specific Governance and Accountability Action Plans (GAAP) Annexes (see for example the Water and Sanitation Service Improvement Project in Kenya (P096367); Federal Roads Development Project in Nigeria (P090135); National Vector Born Disease Control and Polio Eradication Support Project in India (P094360); ID-BOS KITA Project in Indonesia (P107661); Second Health Sector Support Program in Cambodia (P102284)).

8. **Specific actions to strengthen and enhance operation and controls relating to the procurement complaints data base.** Improvements and enhancements have been made to the Bank’s complaints system, which now has enhanced controls relating to complaints entry into the data base and the tracking of follow-up actions. The procurement complaints database has been made a key control and management tool starting in FY07. Since then, OPCPR has been monitoring quality of data and documentation entered in the system and has followed up with the RPMs on its analysis and findings. In addition, enhancements have been made to Web-based Complaint Application on a continuous basis and with full support of the Procurement Sector Board. Specific improvements include: a distinction between complaints related to prior versus post review contacts; facilitation of end-users monitoring of complaints and complaints analysis, through expanded export capacity of the system to Excel sheets; revision of drop-down lists to better reflect the nature of complaints and to allow detection of trends; revision of drop-down lists on the resolution of the complaints (e.g. misprocurement, cancelation) for more accuracy in definition and analysis; automatic reminders to staff to seek RPM clearance when closing complaint cases in the system; automatic alerts to remind TTL, PS/PAS and RPMs of
long pending cases; automatic monthly reports to RPMs on the cases pending longer than 75 business days; and automatic alerts if complaints are pending on projects that are about to close. OPCPR has also strengthened monitoring of complaints follow-up by (i) tracking complaints related to late payments directly with the regions, and (ii) preparing and providing quarterly/semi-annual monitoring reports to procurement senior management.
THE WORLD BANK

IDA: INTERNAL CONTROLS REVIEW:

MANAGEMENT ASSESSMENT FY08

PART II REPORT

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ANNEX A: ENTITY LEVEL CONTROLS

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ANNEX A: ENTITY LEVEL CONTROLS

Executive Summary

1. As set out by the Commission of Sponsoring Organizations of the Treadway Commission (COSO), under the COSO internal controls framework, Management is responsible for establishing and maintaining an effective internal control system. In line with the Scoping Memo of its assessment of internal controls over the International Development Association’s (IDA) operations and compliance with its charter and policies, during Part II, Management focused on: (i) entity-level controls, (ii) outstanding transaction-level controls deferred from Part I, and (iii) whether the internal control framework over IDA operations provides Senior Management and the Board reasonable assurance that they are made aware, in a timely manner, of the extent to which IDA is moving toward effective and efficient use of its resources in meeting its operational objectives.

2. As a result of this work, and work conducted during Part I, Management concludes that entity level controls combined with transaction level controls are adequate to provide reasonable assurance to Senior Management and the Board that:

- IDA’s published financial statements are being prepared reliably;
- IDA carries out its operations in compliance with the relevant provisions of its Articles of Agreement and operational policies and procedures; and,
- They are made aware, in a timely manner, of the extent to which IDA is moving toward effective and efficient use of its resources in meeting its operational objectives.

3. While the Bank’s control environment, risk assessment, control activities, monitoring, and information and communication components of its internal controls framework (as defined under COSO), are deemed to be overall positive, the review pointed up several areas of opportunity for enhancing and strengthening these areas as follows:

A. Control Environment

- Raise staff awareness about appropriate behavior, including providing unit specific voluntary training by staff from the Office of Ethics and Business Conduct (EBC) and online training on ethics issues;
- Strengthen emphasis on ethics and internal controls in HR tools, such as job descriptions and performance evaluations, and review incentives to encourage staff to identify and report corruption-related activities;

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2 Details for the rationale for the assessment can be found in the “Report from the Executive Directors of the International Development Association to the Board of Governors, Additions to IDA Resources: Fourteenth Replenishment, Working Together to Achieve the Millennium Development Goals,” (approved by the Executive Directors of IDA on March 10, 2005), paragraph 39, under the Disclosure bullet.

3 Management’s work on supplemental transaction-level controls deferred from Part I are covered in a separate report, Annex B.
ANNEX A: ENTITY LEVEL CONTROLS

- More systematic feedback from the Department of Institutional Integrity (INT) to Management needed regarding underlying control deficiencies to facilitate real-time adjustments to project implementation;
- To deter inappropriate and improper behavior, consider measures to communicate, on a case-by-case basis, some instances of such behavior;
- Strengthen the linkage between performance evaluation and individual accountability;
- Improve the alignment of staffing levels and skills mix to changing client needs, shifts in demand, new practices, and emerging corporate needs;
- Improve incentives to staff to work across sectors or to address inter-sectoral issues, and strengthen linkages of such incentives to the achievement of the goals of the institution;
- Review areas where the work of central control units could benefit from greater coordination, rationalization and aggregation, and those activities, created to address specific problems, that are not closed in a timely manner, as these may lead to “mission creep”;
- Follow-up on staff survey results (e.g., staff dissatisfaction over rewards for job performance, feedback to strengthen OPE process, etc.); and,
- Note that the Board has identified issues relating to the Board’s internal governance and has commenced a review to strengthen its controls.4

B. Risk Assessment

- Assess mechanisms for linking systemic risks identified from time to time with objectives, initiatives, and business processes, opportunities for alignment and coordination across the institution
- Consolidate risk identification processes and analyses prepared by various units, including the review of reputational and political risks, and identify ways to rationalize and improve effectiveness and efficiency of checks and balances provided by the central control units;
- Introduce measures that would improve timeliness and accuracy of risk identification and information sharing within the task team and between management and staff;
- Explore various mechanisms for better risk aggregation and assessment/review rationalization, including mechanisms in place to validate and prioritize key risks for monitoring and testing as well as defining opportunities for improvements to controls and management activities; and
- Better sensitization of staff and Management to risks to information security posed by password policy breaches.

C. Control Activities

- Review policies and procedures to determine if they can be made less burdensome, including looking at controls over the administrative budget;
- Review oversight of AAA processes, as well as scope for OPCS, CSR, and ISG to work together more efficiently;
- Review controls relating to decentralized procurement; and
- Mainstream and integrate fraud and corruption issues into daily operations (as set out in Management’s Response to the Volcker Panel Report).

4 See “Report to the Board from COGAM green sheet,” July 11, 2007 meeting.
D. Monitoring

- Issues identified were similar to those in control environment and risk assessment sections above.

E. Information and Communication

- Improve data systems to reduce manual intervention and facilitate recovery of consistent aggregated numbers by business units, and their reporting on these to Senior Management and the Board;
- Include in the rationalization of central control units a review of the similarities of information each one gathers or requests from business units, whether these need to be separately collected from business units each time, and how improvements could be made in the timeliness of the transfer of information from business units to central control units;
- Improve user-friendliness of systems and technology links to decentralized offices; and
- Strengthen compliance of business units to unit level business continuity plans.

4. The above conclusions, identified areas for improvement, and recommendations are based on work undertaken throughout the assessment, with particular emphasis on Part II. In this regard, the scope of Management’s work and details of assessment activities undertaken during Part II, including its approach to each activity and methodologies followed to complete such work, as well as specific findings overall (organized by COSO component, to facilitate its review work), are described in the sections that follow.
I. Scope

A. COSO Control Framework

5. As it has throughout this assessment, during Part II management followed the Commission of Sponsoring Organizations of the Treadway Commission (COSO) definition of internal control,\(^5\) namely, a *process* affected by an entity’s board of directors, management and other personnel, designed to provide *reasonable* assurance regarding the achievement of objectives in the three COSO categories of financial reporting, compliance and operations. Management assessed internal controls related to these three objectives against different expectations, an approach that was consistent with COSO. In the context of the financial reporting and compliance objectives, which are primarily within IDA’s own control, management assessed whether IDA’s internal control system can be expected to provide *reasonable assurance* that IDA’s financial reporting is reliable and that IDA carries out its operations in compliance with its charter and operational policies. In the context of the operations objective, however, which is not always within an entity’s control, management assessed whether the internal control system in place provides “reasonable assurance only that *management* and, in its oversight role, the Board, are made aware, in a timely manner, of the extent to which IDA is moving toward its operations objectives.”\(^6\) It is important to note that the distinction between the operations and the compliance and financial reporting objectives was not reflected in the Part II Scoping memo, which set the operations objective in terms of “assessing whether internal controls over IDA operations provide reasonable assurance to senior management and the Board that IDA’s operations are carried out efficiently and effectively”. Management determined the need for this revision upon a closer review of the COSO report which it used to guide its entity-level work relating to this objective. As explained in the COSO Report, since the operational objective is not always within the entity’s control, all the internal control system can provide is a “reasonable assurance ... that management and, in its oversight role, the Board, are made aware, in a timely manner, of the extent to which an entity is moving towards its operations objectives.”\(^6\) This is especially important for IDA, given the many factors outside IDA’s control that may and often do affect the development impact and effectiveness of IDA’s operations. Since this review is likely to become a precedent and set standards for similar work inside and outside IDA, it is important to set a realistic standard for the operations objective in line with the COSO approach. The following is a summary of the scope and methodology followed by management in assessing each of the three objectives against these expectations.


6. Since 1997, management has annually asserted and received attestations from the external auditor that it maintains an effective system of internal controls over external financial reporting for both IBRD (International Bank of Reconstruction and Development) and IDA. The work undertaken by management, and attested to by the external auditor, during the FY07 Internal Controls over Financial Reporting (ICFR) process is described in the annexes to management’s assertion and the external auditor’s attestation for FY07.

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C. Compliance with Applicable Laws and Regulations

7. The corporate entities for which the COSO framework was developed are subject to specific laws and regulations in their respective jurisdictions. IDA’s status as an international organization with immunities and privileges makes this COSO category not directly applicable. However, in addition to its charter (i.e. its Articles of Agreement) IDA has a body of internally generated policies and procedures with which it needs to comply. Management has therefore interpreted compliance with laws and regulations to mean compliance with IDA’s (i) Articles of Agreement, and (ii) operational policies and procedures.

8. Management’s assessment of IDA’s compliance with relevant provisions of its Articles of Agreement and operational policies and procedures was carried out in two parts. During Part I management focused on transaction-level controls relating to compliance with (i) provisions of the IDA Articles of Agreement, as interpreted from time to time by IDA’s Executive Directors, relating to the management of IDA’s lending operations, including provisions relating to the use of funds for intended purposes; and (ii) internal operational policies and procedures relating to the management of IDA’s lending operations. The results of this assessment are set out in management’s Part IB report. During Part II, management assessed entity-level controls relevant to compliance with the Articles of Agreement and operational policies and procedures linking these to the transaction-level controls relating to compliance identified and assessed under Part I (as supplemented by the additional transaction-level work completed during Part II and set out in Annex B to the overall report).

D. Effectiveness and Efficiency of IDA’s Operations

9. Part II of management’s assessment has focused on whether internal controls over IDA operations provide reasonable assurance to Senior Management and the Executive Directors that they are made aware, in a timely manner, of the extent to which IDA is moving toward effective and efficient use of its resources in meeting its operational objectives.7 The transaction-level assessment under Part I yielded important findings that had a significant bearing on, and were reflected in, the overall assessment of internal control over effectiveness and efficiency of operations. The findings and recommendations of this assessment, and the detailed methodology are set out in the Methodology section of this report.

10. In summary, the main tools utilized by management in carrying out an assessment of entity-level controls relating to efficiency and effectiveness of operations included:

- assessment of the Board’s function;8
- preparation and assessment of the ELC Questionnaire (ELCQ) that addressed the five COSO components (control environment, risk assessment, control activities, information and communication, and monitoring and evaluation) as well as anti-fraud and corruption controls;

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7 As explained in paragraph 5, this represents a revision from the formulation of this objective in management’s Part II Scoping memo and aligns it more closely with the COSO standard for this objective.

8 A paper prepared by LEG and SECBO on the Board’s Role, Procedures, and Decision-Making is the Attachment to this Annex.
ANNEX A: ENTITY LEVEL CONTROLS

- review and assessment of the terms of reference, key outputs (including the main recommendations) of the central control units, including documentation and review of the current budget process;
- review of decentralized operations;
- review of application and general computer controls related to information technology;
- documentation and review of the current processes for identification, formulation, approval and implementation of policy revisions needed to reflect changes in IDA’s strategy, priorities, operational model, and identified risks, and
- integration of findings relating to effectiveness and efficiency from transaction-level work conducted under Part I, and particularly findings regarding inefficiency of current processes governing IL operations and work done under Part I to identify and review current processes and tools in place\(^9\) to monitor and report to senior management and the Board at various stages on progress of projects and programs supported by IDA toward achieving the agreed outcomes (both at the project level and at the country level).

II. METHODOLOGY

11. During Part II Management conducted six major reviews that helped Management determine how IDA entity-level controls are functioning, and whether and where there are areas for improvement. Specifically, these were: (a) an examination of the role of the Executive Directors in IDA’s Internal Control Framework, (b) a review of responses to the Entity Level Controls Questionnaire (ELCQ)\(^{10}\) filled out by all senior managers at the unit level, (c) an analysis of the role of Central Control Units, (d) a recapitulation of the Budget Process used to allocate resources in support of objectives, (e) a review of the operation of controls in Country Offices, and (vi) a review of controls exercised through Information Technology (IT) systems. In addition to using these tools, Management also reviewed key findings from the most recent annual reports from Central Control Units, the Volker Panel Report and Management’s Response to this Report,\(^{11}\) the India Detailed Implementation Review (India DIR) and Management’s Response,\(^{12}\) the Staff Survey of 2007, the Risk and Opportunity Workshops (ROWs) and the most recent Risk Scan run by CSR to supplement findings from the above.

A. Assessment Activities

1. Examination of the role of the Executive Directors in IDA’s internal control framework

12. Consistent with the scoping memo for Part II, management has conducted a review of the role of the Board of Executive Directors (the “Board”), its procedures, and decision-making tools. The Legal Vice Presidency (LEG) and the Corporate Secretariat (SEC) were responsible

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\(^9\) These include: progress reports on implementation IL and DPL operations (ISRs) and CAS progress reports, and completion project, DPL and CAS completion reports, as well as IEG evaluation of each ICR, CAS completion reports as well as country and thematic evaluations.

\(^{10}\) See paragraphs 13-19 for a brief description of the ELCQ and the methodology used to review responses received from unit-level managers.

\(^{11}\) See footnote 16 to the Report.

\(^{12}\) See footnote 11 to the Report.
ANNEX A: ENTITY LEVEL CONTROLS

for preparing the document (the “LEG/SECBO Note”, the Attachment to this Annex), which summarizes: (a) the primary control functions of the Board (consistent with its responsibilities under IDA’s Articles of Agreement, as interpreted through various decisions, legal opinions and other means); (b) the main tools, structures and other means for carrying out these functions (including a summary relating to the Board’s committees and their respective roles and functions, types of meetings and other means for deliberation and decision-making; types of Board documents and disclosure regime that applies to the main ones); (c) rules of conduct that apply to Executive Directors and their staff; and (d) more specific information regarding the function/role of the Audit Committee, which has the primary mandate for assisting the Board in overseeing IDA’s financial condition, risk management and assessment processes, the adequacy of governance and controls, and reporting and accounting policies and procedures.

The Board under the auspices of COGAM is currently looking into broader governance issues relating to the role of the Board. While management expects that this review would result in important findings and possible recommendations for improvement in various areas of Board operations, it does not expect the review to identify major gaps or weaknesses in the Board’s function. Management is therefore of the view that COGAM’s review is unlikely to have a material negative impact on management’s current assessment that the Board is functioning properly and is providing the appropriate governance and oversight of IDA’s operations.

2. Review of responses to the ELCQ

13. **Background: Questionnaire design.** Management developed the ELCQ as its main tool in assessing entity-level controls. The ELCQ was based on the COSO Questionnaire used by IDA’s Controller in conducting the annual ICFR exercise. In developing its ELCQ, Management supplemented and expanded the COSO Questionnaire, drawing on information from the public accounting profession and the U.S. Government Accountability Office (GAO).

14. **ELCQ coverage.** Consistent with its overall approach, the ELCQ was divided into sections that corresponded with the five COSO components of internal control: control environment, risk assessment or fraud risk assessment, control activities, monitoring, and information and communication. The five sections contained a total of 145 questions (one question, #56 was broken down into 3 sub-questions (a, b, c)) designed to facilitate Management’s assessment of the Bank’s entity-level controls. These were later supplemented by 12 additional questions that focused specifically on the area of anti-fraud and corruption.

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13 The work on LEG/SECBO Report was prepared and coordinated by Dirk Mathiesson, Manager (SECBO) and Natalie Lichtenstein, Assistant General Counsel (LEG) with assistance from Elisabeth Marmolo, Senior Board Operations Officer (SECBO) and Alex Iorio, Lead Counsel (LEG).

14 The Note prepared contained specific descriptions: for example, with respect to operational policy and strategy, the Board sees, *inter alia*, policy and sector papers; operational policies; country assistance strategy documents; poverty reduction strategy papers and joint IDA-IMF staff advisory notes; general operations (that is, credits, guarantees, and IDA grants). In addition the Note said the Board carries out monitoring and evaluation activities, including reviews by an independent evaluation group (IEG), an Inspection Panel (with respect to certain issues raised by third-parties); and it has a policy on disclosure of information to external parties. Finally, the LEG/SECBO Note pointed out that the rules and practices of the Executive Directors have been continually revised and updated, generally through the mechanism of a Board review of procedures. The most recent review was in the 2005 Report entitled *Board Effectiveness: Making Board Decision-making Processes More Efficient*.

15 COSO published a report in 1994, “*Internal Controls – Integrated Framework,*” Executive Summary. The report is widely referred to by leading financial institutions in the United States and is also seen as a model in many other parts of the world. IDA adopted the COSO framework as its controls methodology in 1995.
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bringing the total of questions to which responses were sought to 157. The questions covered topics suggested in the COSO paper intended to facilitate evaluation exercises.

15. **ELCQ launch.** The ELCQ was launched at a meeting of the Operations Vice Presidents (OVPs) that was co-chaired by the two operations Managing Directors (MDs) Graeme Paul Wheeler (MDW) and Juan Jose Daboub (MDD). The ELCQ was sent to the managers responsible for department-level functions at the Senior Management level: Managing Directors, Vice-Presidents, and Heads of the Quality Assurance Group (QAG), Internal Auditing Department (IAD), Department of Institutional Integrity (INT), General Services Department (GSD), Inspection Panel, and IEG. OPCVP, CSRVP and the project team briefed managers on the context, process, method, and timelines of the questionnaire process. They asked respondents to apply informed judgment in filling out the questionnaire, while selecting one of three responses to each question: “yes”, “no,” or “not applicable (N/A),” except for 16 questions (Q95-Q110), which only IEG, QAG, and OPCS were asked to answer. They also asked participants to substantiate their responses by describing, commenting on, or providing tangible examples of unit or institutional-level actions, practices, or outputs that showed how the issue was addressed, or to record what they observed regarding any problems or gaps.

16. **Review of responses.** In reviewing responses to the ELCQ, including those that were subject to updates by unit managers, the project team took a phased and analytical approach: the team summarized individual questions within each component, analyzed them, and then prepared overall summaries for each COSO component. In preparing both the question-by-question summaries and the overall component summaries, the team included relevant responses from the ICFR process. In reviewing the responses, the team considered whether responses were given from a unit perspective, from the perspective of the institution as a whole, or both. Responses were also classified according to whether they positively reinforced any control(s) referred to in such questions, or whether they reflected control weaknesses. The team then accumulated responses signaling weaknesses or gaps to consider whether IDA’s objectives in a given area were negatively affected. The review process outlined above is explained in further detail in the next few paragraphs.

17. The team conducted follow-on interviews with representatives of individual units that responded to the questionnaire to (a) spot-check Management’s responses to the questionnaire; (b) obtain additional inputs and insights on issues that the project team had identified as needing clarification; and (c) gather any additional information that was not captured in the questionnaire responses. The project team also used these interviews to obtain clarifications on

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16 Early in the process, the project team had realized that the limited number of antifraud- and anticorruption-related questions would not provide sufficient information to allow the project team to form conclusions in this area. Consequently, 12 supplemental questions were added and were attached to a reminder about the deadline; a later deadline was set for the additional set of questions. This brought the total number of questions to 157.


18 The team, led by Galina Mikhlin-Oliver (OPCS) and Yanni Liakakis (CSR), included Rui Manuel Coutinho and Anna Pinto Hebert (OPCS), and David Mead (consultant, OPCS).

19 Following one-on-one interviews or email exchanges with the project team, the senior managers in the following units updated their responses: MDW, Africa, IAD (twice), INT, IEG, GSD and QAG. These updates were important to the project team objective of accumulating relevant and pertinent information.
positions/ responses that were markedly different from those provided by other units; in this effort they sought a better understanding of whether Management as a whole considered entity-level controls to be in place, and whether “outlier” positions were voiced from sources that were closer to the practice of entity-level controls (such as those exercised by central control groups) and thus had a bigger impact on these controls than others. Interviews conducted:

- Africa and South Asia management representatives (these Regions represent the substantial portion of IDA lending)
- IAD (twice), IEG, and INT management representatives (these units are key central control units), and
- HRS management representatives (this unit is a major FAC unit whose activities directly affect staff)

18. Using all the information gathered, the team summarized each question. They applied professional judgment to (a) weigh the importance and source of caveats to capture them in the summaries, (b) substantiate “glass half-full” or “glass half-empty” responses, as applicable, and (c) identify areas in need of improvement. The team then prepared summaries by COSO component based on response received with conclusions on entity-level controls based on the key criteria specified by COSO. As the project team drafted its overall summaries, the team accounted for responses specific to the following units:

- **IEG**: IEG gave “N/A” responses to questions on areas that IEG has not evaluated, since its unique professional standards require that its opinions be based on evaluations.
- **SAR**: SAR intended its “In principle …” responses to be interpreted as positive, with the caveat that while controls or actions referred to in the questions are in place, Management actions or processes in these areas need strengthening. For example, its response to Q#115, “Are desired internal control actions followed up on to implementation?” SAR management responded, “In principle. Through follow up by IAD, QAG and others.” During a one-on-one interview, the manager confirmed that SAR management believes this area indeed needs more monitoring.
- **INT**: Responses that contained both “yes” and “no” statements differentiated INT’s opinions on how half of the response applied to INT as a unit, and how the other half applied to the Bank as an institution.
- **IAD**: Responses that had “?” marks meant that it was unclear to IAD whether its response would be “yes” or “no” for the institution.

19. **Iterative Process.** As might be expected in such a complex exercise, issues and topics surfaced unevenly and at various points throughout the review process. The team also found that the preliminary concepts, components, and criteria it developed from initial data evolved over the course of the review, or as more information was gathered. Consequently several phases were revisited as information and analysis evolved, or as gaps in the information being collected became apparent.

3. **Analysis of central control units and their role in IDA’s internal controls framework**

20. Based on a definition of what constitutes a central entity level control unit in COSO (discussed and agreed with IAD and IEG), namely “A central control unit is an oversight/monitoring unit that performs ex-ante (guidance setting and review of process design) and/or ex-post activities (monitoring/ reviews/ audits) independent of the business
unit being reviewed, to assess the quality and compliance as well as the efficiency and effectiveness of IDA business units’ activities and processes,” Management identified ten central control units and classified these under the following three categories:

<table>
<thead>
<tr>
<th>Management Activity</th>
<th>Office of Ethics and Business Conduct (EBC)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management Oversight</td>
<td>Controller’s group (CTR); Controller’s, Strategy and Resource Management Department (CSRRM); Corporate Strategy and Integrated Risk Management (CSRSI); Operations Policy and Country Services (OPCS); Quality Assurance Group (QAG)</td>
</tr>
<tr>
<td>Independent Oversight</td>
<td>(i) Reporting to Senior Management and Audit Committee: Department of Institutional Integrity (INT); Internal Auditing Department (IAD);(ii) Independent of Management: Independent Evaluations Group (IEG); and the Inspection Panel (IPN).</td>
</tr>
</tbody>
</table>

21. For each control unit, the oversight authority was identified based on the organization chart of the World Bank, information on its website or in its reports or by asking the unit itself. Terms of Reference (TORs) and key reports prepared by each control unit were obtained (the most recent available, which was November 2007 in most cases), as well as the primary audience for each report identified.

22. Each report was reviewed to identify the main areas of coverage and objectives of the report, the main observations, findings and recommendations made and the response by Management to such findings or recommendations, if any.

23. Clarifications and follow-up were sought from staff in the control unit where deemed necessary, usually as part of the OPCS/CTR follow-up interviews/drill-downs on the ELCQ (specifically in meetings with CTR, IAD, INT, and IEG). A matrix setting out the work performed above for each central control unit was also sent to the relevant unit for review and the matrix was updated to reflect the input received.

24. Management mapped each central control unit by COSO component and examined any potential linkages, gaps, overlaps between the roles and outputs of the groups in question and any other issues.

4. Recapitulation of the Budget Process used to Allocate Resources in Support of Objectives

25. In undertaking a recapitulation of the Budget Process, Management noted that while all business units are responsible for ensuring the efficient use of IDA resources in their day-to-day activities, the Controllers, Strategy, and Resource Management department (CSRRM or CRM for short) is the central control unit tasked with ensuring the appropriateness of inputs to enable the Bank through its various business units to achieve the desired outcome. Management found this is achieved through the annual budget allocation process and monitored using the Quarterly Business Review (QBR) process.
26. With CRM’s assistance and existing descriptions and documentation of the budget process, Management analyzed the entity level FY08 budget process carried out in FY07. All key documents were identified and reviewed to ascertain how the budget process allocated resources in support of the corporate and business unit strategies. Management verified that evaluation criteria including benchmarks, historical trends, internal and external comparators, and other knowledge available to the central staff have been rigorously applied to the budget process. This process was then verified with CRM staff.

27. Because of changes in Senior Management in late FY07, the FY08 budget process deviated in significant respects from the planned process: e.g., the FY08 Budget was approved in absence of a multi-year resource framework, allocations to VPUs were significantly delayed resulting in the country-level detailed plans being delayed into FY08, and major components such as the Governance and Anti-Corruption (GAC) agenda were being defined well into FY08. Management noted where these delayed steps had a significant impact during its review. Finally, since the FY09 budget process is already underway with a different approach to objective setting, it is expected that some of the FY08 objectives will be revised during the current year.

28. In undertaking this recapitulation of the Budget Process, Management noted that it recently reviewed with the Board the current state of the budget process and its proposed action plan to make the process even more effective and transparent in the future. Details on this effort were described in the Board paper: “Improving the Planning, Budgeting and Performance Management Process,” dated October 9, 2007, incorporated into this review by reference. Management’s review therefore focused on describing the FY08 budget planning process from a COSO perspective, and specifically on the entity level processes to allocate resources in support of corporate and business unit strategies and not on the related sub-entity unit specific level processes. With regard to the latter, Management noted at the outset that the budget process was heavily country-driven and that the controls surrounding the Country Assistance Strategies (CASs) have been reviewed and assessed during Part I.

5. Integrating Part I findings relating to efficiency and effectiveness

29. While Part I focused on assessing a compliance objective at the transaction level, it also included a review of processes and tools that have a direct bearing on and/or are used to monitor efficiency and effectiveness of IDA’s operations. These include: (a) review of processes underlying IDA operations and a finding regarding their inefficiency and the need for introduction of a risk-based approach as a basis for their rationalization., and (b) review of current processes and tools in place to monitor and report to senior management and the Board at various stages on progress of projects and programs supported by IDA toward achieving the agreed outcomes (both at the project level and at the country level). These tools and processes

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20 Staffing plans are not part of the budget process (or this review), although they are monitored independently. Management also did not review how Trust Funds are allocated to complement the Bank’s budget in achieving objectives. It is important to note, however, that Management has recently developed, and the Board has approved, a new framework for the management of Trust Funds which envisages integration of budgetary and BETF (Bank Executed Trust Fund) resources; in this regard, information on BETF is now included in all budget related reports as a first step.

21 CRM staff consulted included Grant Cameron, Adviser, CRM; Marie H.R. Bakker, Manager, CRM and Glenn Miles, Director, CRM.
include instruments for reporting progress (ISRs and CAS Progress Reports), self-evaluation at completion of CASs and projects (the ICRs and CAS completion reports), independent evaluation of all completion reports by IEG as well as thematic/sector, country, and instrument evaluations by IEG. We have also examined IAD and QAG reports that are relevant to the question of monitoring and reporting, including in particular the recent IAD audit of supervision reporting that focused on project ISRs.

6. Fraud and corruption

30. Upon IAD’s recommendation, during Part II, Management: (a) assessed controls over fraud and corruption at the entity-level through the ELCQ, including controls to ensure that issues identified by fraud and corruption investigations are adequately addressed; and (b) linked, as appropriate, the entity-level fraud and corruption controls identified to the process or transaction-level controls designed to prevent or detect fraud and corruption. As a result of this work, Management developed a listing of specific fraud and anti-corruption controls that have been identified at the transactional as well as entity levels. In performing its assessment, Management considered the findings contained in the Volcker Panel Report relating to fraud and corruption controls specifically and the impact of these findings on the entity-level controls more generally.

7. Review of the operation of controls in country offices

31. IEG recommended and Management agreed that decentralized operations were an increasingly important part of IDA’s operational model and, therefore, should be included in the scope of the overall assessment. To this end, the application of internal controls over IDA operations at the Country Office (CO) level have been reflected in the work completed to date at the transaction level as follows:

- During the review of internal control over financial reporting (ICFR), Management confirmed and the external auditor attested that: (i) all significant disbursement and procurement transactions include those from COs and are captured in the Bank’s systems and tested from headquarters; and (ii) all disbursement approvals are performed in headquarters and all related controls have been tested in headquarters.
- During Part I of the IDA Internal Control Review, the document sample used to perform compliance testing of processes and key controls that apply to the Country Assistance Strategy (CAS), Investment Lending (IL), and Development Policy Lending (DPLs) specifically included transactions (operations) that were task-managed from COs and/or documents that were initiated, prepared and/or reviewed in COs; and
- During Part II, Management:
  - Included specific questions in the ELCQ related to country offices in order to assess whether and how the application of the COSO components of IDA’s internal controls framework extends to these offices; and

22 Management followed the definition of “fraud” in SAS 99: “...an intentional act that results in a material misstatement in the financial statements that is the subject of an audit. Two types of misstatements are relevant to the auditor’s consideration of fraud – misstatements arising from fraudulent financial reporting, and misstatements arising from misappropriation of assets.”
ANNEX A: ENTITY LEVEL CONTROLS

- Reviewed IAD’s reports of audits of country operations completed in FY07 and in the first quarter of FY08 and took them into account in assessing the application/compliance with internal controls at the country-office level.

32. At the conclusion of these reviews, Management found three main areas needing improvement:

- Areas of project supervision, especially project supervision reporting
- Processes and controls in the Procurement; and
- Processes and controls over the Financial Management (FM).

33. These issues are consistent with those identified during the compliance testing and quality reviews of the Procurement and FM processes (please see Annex B for details).

8. Review of controls exercised through information technology (IT) systems

34. During Part II, Management assessed the key IT controls supporting IDA operations. This assessment included all major IT systems used by Bank staff in performing activities related to IDA. The majority of these systems were reviewed during the FY07 ICFR.

a. Integrated systems reviewed

35. In order to ensure that all IT controls related to key processes have been reviewed, Management identified the entire population of integrated IT systems and individual databases used by business units to support IDA’s operations together with the specific business process, the supporting underlying system applications and the applicable underlying technology or software being used. These applications were further reviewed against the objectives of: (a) application systems implementation and maintenance; (b) information systems security; (c) information systems operations; (d) systems software support; (e) network support; (f) database implementation and maintenance; and (g) transaction level controls.

36. These objectives were reviewed and associated controls tested for all the identified key IT systems during the FY07 ICFR review to assess whether such internal controls are adequate to ensure their operating effectiveness. During this review no material weaknesses were identified. However, certain processes surrounding password policy breaches, information security rationalization and monitoring of changes, and change management controls were identified as significant deficiencies requiring Management’s attention.

b. Non-integrated systems identified and reviewed

37. During Part I Management found that many of the process controls that apply to IDA operations at the transaction-level (and particularly to the processes of CAS, IL and DPL) are not automated or do not otherwise entail consistent IT support. The linkage between this finding and the issue of document accessibility identified in Part I have led to the establishment of a working group to look into automation of work flow documentation and controls. Since this relates to future work, there is little that can be assessed during Part II. The one area where limited automated controls were introduced relates to the IT controls relating to supervision reporting through the Implementation Status and Results Report (ISR).
38. In addition to the integrated IT systems and their related controls reviewed during the ICFR, Management identified the processes that required a certain level of system technology, and assessed their impact on internal controls. Management found that the following processes/systems were either not yet operational or fully integrated systems or were not being consistently updated by Regional staff:

- **ISR**;
- **RAPMAN-PRIMA** – the regional integrated FM Portfolio & Risk Management Application for monitoring critical aspects of FM project performance and portfolio management tool;
- **Audit Reports Compliance Database (ARCS)** – the tool monitoring Bank-wide audit compliance; tracking project audit reports due, timeliness, qualifications etc; and audit compliance data is an important indicator of Project FM performance; and
- **Procurement Complaints Database** – the Regions’ system for logging procurement-related complaints as well as for tracking pending complaints etc.

39. Management believes that all of the above systems warrant further review and/or redesign in order to be assessed as entity-wide processes and reviewed for their design and operating effectiveness. Management has included the issues related to these systems as deficiencies arising from Part II and included them in the final deficiency tracker shared with IEG and IAD, with appropriate action plans.

9. **Response to recommendations for Part II Work in the IEG Part IB Evaluation Report**

40. In developing the tools above and in considering findings from other reviews, Management also considered recommendations contained in the IEG Evaluation Report on Part IB. To address these issues, as suggested by IEG, Management tied its findings in these areas to COSO components as follows:

- To address non-compliance occurrences in transaction-level controls that were found during Part IB, and to determine whether these were mitigated, Management linked entity-level controls review work during Part II, which included (i) its reviews of responses to the ELCQ, (ii) the analysis of Central Control Units, (iii) the examination of the role of Executive Directors, and (iv) the review of Country Offices to the non-compliance occurrences. In particular, Management captured its findings in the overall summary on the Control Environment at the entity level, where greater management oversight may be called for.

- To address the significant deficiency found regarding document retention and accessibility, Management linked recommendations from a special Task Force that was put together to examine this area, to controls captured in both the Control Environment and Information and Communications areas at the entity level, where improved IT systems may be part of the solution.

- To address the potential material weakness identified in Part I regarding dated Operational Policies (OP)/Bank Procedures (BP), Management linked process mapping work and its

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24 See paragraphs 41-49 for details.
recommendations to improve operations policy updating to controls related to Control Activities at the entity level, as they are an essential element of the Control Activities component.

- To provide the element of effectiveness and efficiency that was not fully captured in Part I work, Management linked (i) its review of responses to the ELCQ, (ii) its analysis of Central Control Units, (ii) the recapitulation of the Budget process, (iii) a review of controls operating in decentralized operations (in Country Offices), and (iv) additional transactions controls mapping and compliance testing to Control Environment and Monitoring controls at the entity level, and added resulting analysis from these various pieces to results from Part I.
III. Findings

Entity Level Controls by COSO Component

41. The following represents the key IDA entity level controls/processes identified and assessed by Management during the Entity Level Control Review part of the IDA internal control review. The Entity Level controls have been organized by the five COSO components which also include findings relating to anti-fraud and anti-corruption activities.

A. Control Environment

42. Control Environment provides an atmosphere in which people conduct their activities and carry out their control responsibilities. It sets the tone of the organization, influencing the control consciousness of the staff. It is the foundation for all the other components of internal control, providing discipline and structure. Control environment factors include the integrity, ethical values and competence of the entity’s staff; management’s philosophy and operating style; the way management assigns authority and responsibility, and organizes and develops its staff; and the attention and direction provided by the Board of Executive Directors.

43. These controls/processes/activities help review the tone of the organization and represent the foundation for all other components of internal control. Based on our review of the control environment questionnaire responses, the Bank’s control environment is deemed to be overall a positive one. The review pointed up several areas of opportunity for enhancing and strengthening the control environment, and Management will include them in its overall action plan to strengthen its organizational controls. The Control Environment can be broken down into several distinct parts:

44. Integrity, ethical values, and behavior of key executives. In assessing this part, Management considered responses to the Entity-Level Questionnaire (ELCQ); the Office of Ethics and Business Conduct (EBC) Annual Report 2007; ROWs; the ICFR Questionnaire; the Volcker Panel Report (VR) and Management’s Response to the VR; and the Staff Survey (2005, 2007).

(a) Standards of professional conduct have been codified in the Bank’s Staff Manual and are communicated to staff prior to joining the Bank. New staff are required to sign-off on their understanding of Principle 3 upon reading it as an attachment to the Appointment Letter prior to joining the Bank. A mandatory induction course includes specific sessions addressing the code of conduct and ethical behavior. The Bank’s Code of Professional Ethics (the Code) is currently in the final stages of revision and is expected to be approved by the President shortly. The Bank has ongoing efforts to raise staff awareness about appropriate behavior including providing unit specific voluntary training utilizing EBC staff and online training on ethics issues. The available Ethics training clearly identifies unacceptable behaviors and the penalties that result from infractions. It remains the responsibility of individual staff to understand and uphold the Bank’s ethical standards.
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(b) Although Management’s commitment to integrity and ethical behavior is communicated effectively in words, and the Staff Survey (2007) results indicated 81% of staff believe their managers act with honesty and integrity, a few Respondents felt that in deeds it has been less clear [IAD, EBC]. In light of the recent ethics-related situation involving the former President, staff and managers have raised questions (for instance, in their postings on internal communication sites and in their communications to EBC) that this area requires considerable strengthening [EBC, HRS]. A positive outcome is an increased emphasis on ethics training, as an increasing numbers of managers are seeking advice from EBC and are requesting ethics training for their staff.25

(c) Rewards can foster an appropriate ethical tone when given to staff members who accomplish objectives while respecting established policies, procedures and controls. However, because the rewards available to Bank staff (salary increases, spot awards, promotions, and assignments) are limited, they are not considered to have a significant impact in promoting ethical behavior among staff [MDD, EAP, EBC, INT, EXT, HRS]. Although some emphasis is now being placed on behaviors, there is no systematic review of behavior. Far greater recognition is given to results in annual performance evaluations. Management has no reason to believe that the current system systematically rewards the circumvention of established policies.26

(d) Management acts to remove or reduce incentives or temptations that might prompt staff to engage in dishonest, illegal or unethical acts by amending and changing internal policies, processes and procedures when required and strengthening controls. However, this area would specifically benefit from more systematic feedback from INT to Management regarding the underlying control deficiencies supporting their findings in order to enable Management to identify systemic issues and correct incentives for misconduct as well as focus attention to these issues by all Bank units. Program integrity requires far more than the effective functioning of INT.

(e) There is also a well-defined and broadly understood process in place to handling employee claims and concerns in a relatively timely manner (always depending on the type of claim or concern).27 However, the results of reviews/investigations and findings of subsequent misconduct are not always communicated in a Some of these concerns are being addressed by ongoing activities in the accountability and ethics areas, such as emphasis on ethics and controls in the orientation program provided for all new Bank hires and

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25 EBC has identified that the number of staff cases seeking advice on ethical dilemmas and conflicts of interest has increased 77% from FY05 to FY06.
26 In ROWs, staff across the Bank report that they feel individual staff and units are primarily rewarded for specific results such as project delivery to the Board and project completion with less attention paid to the method or quality of these achievements. As an example, INT investigations have identified instances where deficiencies in projects did not negatively impact the staff involved. In their submissions to the ICFR ELCQ, EBC and INT reiterated their concerns that individual staff and units are primarily rewarded for specific results such as project delivery to the Board and project completion with less attention being paid to the method or quality of these achievements.
27 Some issues may take longer given the need to ensure due diligence in the investigation process.
implementation of appropriate disciplinary action in response to departures from approved policies and procedures or violations of the code of conduct pursuant to Staff Rule 8.01. In addition, the Bank has recently amended the Principles of Staff Employment to enhance its current handling of whistle-blowing reports and claims of whistle-blowing retaliation. The new principle and staff rule puts the Bank Group at the leading edge of whistle-blowing protections amongst international organizations, consistent with the highest standards of good governance and the on-going efforts of the Bank to safeguard its integrity and effectiveness. Consistent manner, as the need for confidentiality and privacy typically guide the extent to which the specifics of improper behavior are communicated to staff. Disciplinary actions undertaken in response to improper behavior have not in detail been communicated widely (usually limited to staff on a “need to know” basis and senior management) except in very high profile cases. This may result in a sense that the concerns have not been really resolved or that Management does not care to discipline offenders.

45. **Management’s control consciousness and operating style.** In assessing this part, Management reviewed the responses to the ELCQ:

(a) Management endorses the use of performance-based management, which is the key principle VPs use in managing their business units. There have been significant efforts to incorporate performance-based management into planning and monitoring practices with some units using performance-based management in the measurement of annual results through Results Agreements between managers and the VP, and in the OPE discussions.

(b) In the Regions, at the level of the SMUs and CMUs, the Regional Management Team chaired by the Regional VP regularly discusses key performance indicators, including strategic staffing, deliverables and budgets, as well as strategic priorities and program implementation.

(c) At the Staff level, performance management is provided through the OPE process, SRI and promotion decisions. However, the implementation is impacted by HR policies and procedures, which could benefit from a stronger linkage between performance evaluations and individual accountability: for example, job descriptions and performance evaluations do not contain specific references to internal control related duties, responsibilities, and accountability. Although these are sometimes addressed in the individual OPE depending on the staff work program, references tend to be general for most non-managerial positions.

(d) Management recognizes that emphasizing the importance of integrity and ethical values in the performance evaluation process is subject to the abilities of each manager. Although controls are viewed by Senior Management as the

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28 On the broader issue, that is not just confined to internal controls, the Staff Survey 2007 found that assessments on rewards, performance management and career opportunities continue to be persistently weak, with high levels of dissatisfaction over objectivity and transparency.
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responsibility of line managers, line managers vary in their abilities to discharge their control responsibilities. As with all policies related to staff compensation, performance evaluation and promotion, constant monitoring and feedback is required to strengthen them. However, the implementation of this feedback is again subject to the abilities of each manager. For these and other related reasons, the primary focus of the HR Renewal process currently underway is on strengthening performance management in the Bank.

46. **Management’s commitment to competence and adequacy of resources.** In assessing this part Management reviewed the responses to the ELCQ.

- Management is committed to recruiting and maintaining competence (excellence) in staff. However, there is some concern that the current staff levels and skills mix needs to be better aligned with changing client needs and shift in demand. In this connection, it was noted that changes in skills mix in order to meet changing client needs are not easily implemented and continuous effort is required to adapt skills mix to respond to business needs. Staffing levels and skill mix are reviewed and plans adjusted at least annually, and on a quarterly basis in some units. The majority of Respondents to the ELCQ described their departmental staffing levels as appropriate. Several noted that decentralization and time differences impose additional burdens on staff. [AFR, PRM, IAD, CFP, HRS, LEG]. Two control units [IAD, INT] responded that they do not have sufficient resources to complete their work, or in INT’s case to fully deliver on its mandate.

47. **Board of Directors.** In assessing this part, Management reviewed the Paper prepared by LEG/SECBO on the Board’s Role, Procedures and Decision Making, the FY07 COSO Report and ROWs.

(a) As part of this Part II Entity-Level Control assessment, Management identified the primary functions of the Board, particularly as they relate to “tone at the top,” ethics and culture, and with respect to IDA’s overall internal control framework.

(b) The Bank has a unique governance structure with a full-time sitting Board. Management is aware that the Board has identified issues relating to its internal governance and has commenced a review to strengthen its controls. In light of ongoing work by the Board in related areas, Management did not go beyond identification of the Board’s primary functions. The paper prepared by LEG/SECBO contained specific descriptions: for example, with respect to operational policy and strategy, the Board sees, inter alia, policy and sector papers; operational policies; country assistance strategy documents; poverty

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29 To be reviewed during HR Reform.
30 See Attachment to this Annex, “Board’s Role, Procedures, and Decision Making.”
31 See, Report to the Board from the COGAM green sheet, July 11, 2007 meeting.
32 As stated in page 5 of “Management’s Scoping Memorandum, Part II” (Annex C to the Report), Management has noted that a Sub-Group on Governance (SOG) was established by COGAM “to examine issues directly related to the recent leadership crisis, and broader issues of potential risk in other areas of the bank’s governance arrangements,” from Report to the Board from the COGAM green sheet, July 11, 2007 meeting.
reduction strategy papers and joint IDA-IMF staff advisory notes; general operations (that is, credits, guarantees, and IDA grants). In addition the paper pointed out that the Board carries out monitoring and evaluation activities, including reviews by an independent evaluation group (IEG), an Inspection Panel (with respect to certain issues raised by third-parties); and it has a policy on disclosure of information to external parties. Finally, the LEG/SECBO paper pointed out that the rules and practices of the Executive Directors have been continually revised and updated, generally through the mechanism of a Board review of procedures. The most recent review was in the 2005 Report entitled Board Effectiveness: Making Board Decision-making Processes More Efficient.

(c) A review of the items set out in (a) and (b) above were sufficient, in Management’s view, to provide reasonable assurance overall that the policies and procedures of the Board of Executive Directors are adequate to provide reasonable assurance that the Board is properly functioning and is providing the appropriate governance and oversight of IDA’s operations; with the qualification that Management’s conclusion may need to be revisited after the internal review by COGAM and SOG has been completed, and their findings have been reviewed and analyzed.

48. **Organizational structure and assignment of authority and responsibility.** In assessing this part, Management reviewed the responses to the ELCQ; the Paper prepared by LEG/SECBO on the Board’s Role, Procedures and Decision Making; ROW’s; Risk Scan; the Volcker Panel Report and Management’s Response; and the matrix of the responsibilities of the Control Units.

(a) Key areas of authority and responsibility have been defined and communicated throughout the organization and appropriate and clear internal reporting relationships have been established. The arrival of a new President and appointment of a third Managing Director (MD), together with the realigning of MD responsibilities will require further review in the next year to see whether the role of a MD role will be one of advisor or manager. Decision-making is clearly linked to assignment of authority, and the level of escalation for decision-making is clear with individuals being held accountable by their direct supervisor for decisions. There are several checks in the system including peer reviews, cross matrix management and procedures for adding value and input through out the process. However, some staff feel accountability can be diffused by the number of reviews and the difficulty in holding staff accountable for projects which have long completion times and may have been assigned to multiple TTLs and managers.

(b) Although most ELCQ Respondents stated that internal reporting relationships were clear, the review of the control units showed some concern that the matrix in the Regions was not functioning as well as it could: Sector Managers say the Country Management Unit is client government driven rather than what will truly enhance development in the country, while Country Managers say that the sectors are protecting their own agendas and staff rather than focusing on the Country Assistance Strategy. The budget process within the matrix is time
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consuming. Finally, the ARDE indicated that achieving results in a given sector may require removal of constraints in other sectors, that is, IDA’s matrix management structure does not provide sufficient incentives to work across sectors or to address inter-sectoral issues.

(c) The Terms of Reference and Reports of the Control Units [IAD, INT, QAG, IEG, and CSR] indicated a mission creep and potential overlap of such units.

(d) With respect to decentralized operations, the majority of Respondents believe they are adequately supervised and monitored. However (i) AFR responded that IAD Reports during the last year suggest that oversight in country offices tends to be weaker than in Washington, and (ii) INT investigations and outside reviews and audits have found deficiencies in supervision and monitoring of decentralized operations, with procurement an area of particular concern.

49. **Human resource policies and practices.** In assessing this part, Management reviewed the responses to the ELCQ; ROWs; Risk Scan; and 2005 and 2007 Staff Survey.

(a) The Bank has comprehensive policies in place that focus on assuring that the best candidate is selected for a given position, and that candidates for promotions are approved by both their internal managers as well as external managers to reduce any potential bias. Compensation, promotion, and rotation policies are based on achievement and performance through annual performance evaluations and management reviews. INT noted that within the Bank promotion is not closely linked to project performance or outcomes but to project approvals. Management also noted that during the recent Staff Survey (2007), their were high levels of dissatisfaction over objectivity and transparency, with only a third of Staff perceiving that they are rewarded according to their job performance. With respect to and ELCQ question on candor and constructiveness of job performance counseling, the only respondent to say “no”, was an MD who commented that career counseling is an institutional weakness, and managers are typically reluctant to take decisive action vis-à-vis poor performers. [MDD]

(b) Several ELCQ Respondents [EAP, ECA, HDN, IAD, HRS] pointed out that the importance of integrity and ethical values are not explicitly identified in the OPE. Although these values are not a systematic element of the Bank’s formal evaluation processes, the importance of personal integrity and ethical values is implied in the behavioral assessment categories of the OPE: client orientation, drive for results, teamwork, learning and knowledge sharing, sets high standards for self and commits to organizational goals. As noted earlier, the emphasis of the importance of these values is subject to the abilities of each manager and is highly dependent on the reviewer’s personal and cultural views on the importance of integrity and ethical values.

(c) At the end of 2006, there were two risks that the Risk Scan rated as high: (i) staff skills and mix, and (ii) resource deployment. Highly restrictive HR policies contribute to the skill mix issues and inability to deploy staff to priority activities.
These concerns seem to be borne out by the results of the 2007 Staff Survey, as Staff assessments of career opportunities continue to be persistently weak.

(d) Management has long-recognized the challenge of managing performance in the Bank—which is key for promoting individual and professional accountability. This has been emphasized most recently in the Report of the Performance Management Working Group published in July 2007. Prompted by the Report, HRS launched HR Insight, a new website dedicated to sharing HR-related data, information and research with Bank Group staff. Efforts have also been made to exercise more differentiation in the recent SRI awards, to ensure that high performers are rewarded. HRS will also develop a comprehensive roadmap/strategy for enhancing performance based on the diagnosis of the root causes of dissatisfaction with current performance management, developed by the Performance Management Working Group, and continue its efforts to enhance the HR Insight website to increase further the transparency of HR-related data.

50. **Fraud and corruption.** In assessing this part, Management reviewed the responses to the ELCQ; INT’s Annual Report (FY2007); the Volcker Panel Report; Management’s Response to the Volcker Panel Report; the draft Whistleblower Policy; and Staff Rule 8.01.

(a) The control environment questions focused on mechanisms in place to report and follow up on allegations of fraud and corruption. Most units responded that IDA has good overall communication channels/mechanisms in place for reporting fraud and corruption matters to the appropriate/responsible parts of the Bank (INT, IAD, EBC) through hotline, staff/manager relations, and other means.33

(b) Some ELCQ Respondents mentioned that a gap exists in the absence of a revised Whistleblower Policy and emphasized the need to put it in place quickly to alleviate Staff’s fear of reprisals.34 However, INT noted that the incentive structure within the Bank does not reward the identification of lapses in procedures and ethical standards, and that there should be awards to Regional Staff who identify and report corruption. Instead, INT believes that staff fear retaliation by managers.

(c) Nevertheless, some confusion remains among staff regarding what to report to whom, that is, the line manager, VPs, IAD, INT, or EBC. Management’s message regarding the importance of ethics and proper behavior is weakened partly as a result of confidentiality and the resulting lack of factual information on the outcome of reported issues. This may be evidenced by the lack of disciplinary information on staff misconduct cases from HRSVP. Finally, as noted earlier, concerns relating to decentralized operations have been raised by IAD and INT regarding lack of rigor and quality arrangements in the oversight by Washington of fiduciary (primarily procurement and financial management) activities.

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33 Staff Rule 8.01 was cited as a source for “what to report and to whom.”
34 More information with respect to the Whistleblower Policy is set out in paragraph 81 under the Information and Communication component.
(d) Some of these concerns are being addressed by ongoing activities in the accountability and ethics areas, such as emphasis on ethics and controls in the orientation program provided for all new Bank hires and implementation of appropriate disciplinary action in response to departures from approved policies and procedures or violations of the code of conduct pursuant to Staff Rule 8.01. In addition, the Bank has recently amended the Principles of Staff Employment to enhance its current handling of whistle-blowing reports and claims of whistle-blowing retaliation. The new principle and staff rule puts the Bank Group at the leading edge of whistle-blowing protections amongst international organizations, consistent with the highest standards of good governance and the on-going efforts of the Bank to safeguard its integrity and effectiveness.

B. Risk Assessment

51. Every entity faces a variety of risk from external and internal sources that must be assessed. A precondition to risk assessment is the establishment of objectives, linked at different levels and internally consistent. The risk assessment is the identification and analysis of relevant risks to achievement of the objectives, forming a basis for determining how the risks should be managed. Because economic, industry, regulatory and operating condition will continue to change, mechanisms are needed to identify and deal with the special risks associated with change.

52. The following controls/processes ensure the identification and analysis of relevant risks to the achievement of IDA’s operations objectives.

53. **Entity-level objectives are established, communicated and monitored.** In assessing this part, Management reviewed the responses to the ELCQ, the Budget Process, and review of tools for monitoring progress, quality and evaluating development impact at exit during Part I.

(a) Many responses to the ELCQ mentioned the Medium-Term Strategy and Finance (MTSF) paper, the Budget Document, and the President’s speech at the Annual Meetings as vehicles used to communicate to staff the priorities and directions for the coming year. In accordance with the Bank’s strategy, each Region sets its own strategy, mission objectives, and goals, reflecting Regional characteristics and the needs of member countries. The Board reviews these strategies. Each VPU prepares a Strategy and Performance Contract (SPC) outlining its objectives and strategies, and, in principle, updates it every quarter. The achievement of the objectives is monitored by the VPU’s themselves (using measurable outcome indicators) as well as through such mechanisms as the Quarterly Business Reviews (QBRs). CASs and Country Partnership Strategy (CPS) exercises update strategic plans at the country level and feed into Regions’ annual SPCs. Management periodically reviews the above plans: annually for the MTSF, quarterly for the SPCs via the QBR process, and every 3-4 years for the CAS. Feedback to Management relating to Staff’s understanding of objectives is provided through different channels, including staff surveys, ROW workshops and formal OC meetings related to CASs. Although

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35 An example are the Six Strategic Themes announced by the President in the Fall of 2007.
feedback is received through several channels, some units mentioned the need for more regular feedback from staff [EAP, HDN, AFR, IEG].

(b) Respondents noted that the alignment between entity-wide and unit-wide objectives is broadly adequate. Senior Management regularly discusses the different strategic documents, and efforts to align strategic plans with entity-wide objectives are evident at different levels of the institution: MTSF, Sector Strategy Implementation Updates (SSIUs), SPCs, CASs. Respondents also pointed out that progress was being made on strengthening the links between resource allocation and institutional objectives through the SPC process. Respondents pointed out that activities are linked directly or indirectly to corporate objectives through unit plans that contain key performance indicators (KPIs). The level of detail increases from the entity level (MTSF and Budget Document) to the unit level (SPCs) and the country level (WPAs). Indicators and work programs are periodically updated and analyzed through the QBRs and SPCs. Some units [PREM, SDN, HDN, WBI] stated that in some cases resources available to achieve objectives are not adequate, that the link between strategy and resources is sometimes elusive [LEG], and that the budget could be better linked to results [MDD]. A few areas are perceived to be not well linked to entity-wide goals [AFR, LAC]. It was also mentioned that some activities, created at a given point in time to address specific problems, may not be closed in a timely manner, leading to “mission creep”, and the need for further progress in results measurement [INT, MDD].

(c) During Part I management identified processes and tools in place to monitor and report to senior management and the Board at various stages progress of projects and programs supported by IDA toward achieving the agreed outcomes (both at the project level and at the country level). These tools and processes include instruments for reporting progress (ISRs and CAS Progress Reports), self-evaluation at completion of CASs and projects (the ICRs and CAS completion reports), independent evaluation of all completion reports by IEG as well as thematic/sector, country, and instrument evaluations by IEG. Management has also examined IAD and QAG reports that are relevant to the question of monitoring and reporting on progress and outcomes, including in particular the recent IAD audit of supervision reporting that focused on project ISRs. This review identified that the processes, instruments and controls in place, including the robust independent evaluation of outcomes by IEG, are generally working well. The review also agreed with the IAD findings, however, that improvements are needed in the progress reporting area by revising the form and use of the ISR.

54. **Management has established mechanisms for identification of risks, and evaluates and mitigates risks appropriately.** In assessing this part, Management reviewed responses to the ELCO; the Budget Process; ROWs; Risk Scan; and the CAS and individual project review processes.

(a) The Bank has in place several mechanisms to assess risks at the entity-level (Risk Scan; ROW workshops) and transaction-level (CAS, lending operations). These
are discussed by Management, including Senior Management, at various times throughout the year. Many ELCQ Respondents mentioned the annual Risk Scan, which covers 40 different categories of risk, as a key tool for risk assessment, and noted as well, the role played by operational reviews. Risk identification also takes place through COSO workshops, Risk Scans, and planning discussions at the Senior and VPU Management levels covering various types of risk. At the instrument level, risk identification is an explicit and central element of the CAS and lending operations review processes. For investment lending a risk identification worksheet is applied. However, it was noted also that the Risk Scan is prepared in different ways across units, and that may lead to inconsistencies [HDN]. The need for better capacity to assess political risk was suggested, as well as the need for more attention to implementing mitigating measures [WBI].

(b) The review of control units pointed out that there is (i) no systemic process to consolidate the various risk identification processes and analyses that are prepared by various units throughout the organization, including a lack of a coherent process for consolidation and identification of key entity-wide/systemic risks and their review and discussion with Senior Management and the Board, and (ii) a need for a more systemic review of and better capacity for assessing reputational and political risks.

(c) There is scope for improvement on risk assessment and feedback/incorporation into project design. Under-reporting of risks is a major issue identified by QAG as it reduces the reliability of portfolio performance indicators. QAG notes that such indicators are no longer as meaningful for tracking and managing portfolio performance because of frequent failure in the ISRs to trigger risk flags. The lack of candor in ISRs is especially troubling as Management relies heavily on the indicators of projects at risk, the fact that they may be flawed and systematically understate risk raises a concern about assertions on the effectiveness of IDA’s operations.

(d) Finally, with respect to risk mitigation, it is interesting to note that while robust information security was among the lowest rated risks in Risk Scan, an IAD audit identified IT issues over information security and infrastructure change management, combined with password policy breaches in SAP by Bank staff, as serious risks that were deemed in aggregate by the Peer committee to constitute a significant deficiency (ICFR). This huge difference in risk perception between IAD and other parts of the Bank points to the need for better sensitization of staff and Management to these risks.

55. Management has implemented mechanisms to anticipate, identify, and react to changes. In assessing this part, Management reviewed responses to the ELCQ, the Budget Process, ICFR, ROWs, and Risk Scan.

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36 For example, panelists in the QSA 7 sample identified more than three times more risk flags on projects than were signaled by ISRs.
(a) Attention is given to risk factors when the institution considers entering a new business line or to create a new product. The Board is highly involved in the process and is also kept abreast of budgetary trends in the course of the year and of the impact of key external events at the global and the country level. The risk that Staff skills mix do not match new practices and emerging corporate needs was mentioned [SDN]. With respect to timeliness, one MD mentioned the need to improve how quickly developing risks are brought to Senior Management’s attention [MDD].

(b) However, the ICFR raised the point that the central units could work better together on risk identification and response to risks and information sharing. IDA could strengthen its high-level risk management, by periodically and systematically reporting top level finding to Senior Management.

(c) In addition, INT expressed concerns (which also related to their responses under the Control Activities section of the ELCQ) about whether institutional goals were correct or followed, responding, for example: “The Bank reviews performance measures; the Bank does not always completely validate the propriety and integrity of these measures...the Bank’s business model has inherent limitations”. Management has also identified these issues as part of its ongoing review of the efficiency and effectiveness of the budgeting processes. Along with a number of other issues, they are included in the Management Action Plan which was presented to the Board in October 2007, in the Budget Committee paper “Improving the Planning, Budgeting, and Performance Management Process” (BC2007-0015). Progress on implementing the Action Plan is reported to the Budget Committee through the Quarterly Business Reviews.

56. Fraud and corruption. In assessing this part, Management reviewed the responses to the ELCQ; INT’s Annual Report FY2007 the VR, and Management’s Response to the VR.

(a) In the area of fraud risk assessment, VPs agree that they consider and assess the potential for fraud and corruption as part of their enterprise-wide Risk Scan. In addition, ROWs, IAD audits, and unit-specific risk scan exercises were frequently cited as the primary tools used to assess these issues at the business unit levels.

(b) Most VPs believe that unit-level controls in the fraud and corruption area are effective, citing: (i) unit-level controls put in place by RM teams; (ii) controls embedded in SAP; (iii) institution-wide initiatives and assessments, including ROW; (iv) the Quarterly Business Reviews; (v) Risk Scan Exercises; (vi) Letters of Representation (LOR); (vii) random audits conducted by IAD, external auditors; and (viii) the on-going Quality Assurance Reviews conducted by ACT. However, INT responded in the ELCQ that “The incentive structure within the Bank does not reward the identification of lapses in procedures and ethical standards. There should be awards to regional staff who identify and report corruption; instead, many staff fear retaliation by managers.”

(c) As noted, Management’s individual risk assessment processes include assessment of fraud and corruption risks, however, two control units [CSR, INT]
highlighted that a systemic entity-wide aggregation of the assessed fraud risks is lacking. Finally, IAD stated that systematic risk assessments form part of its own annual risk assessment, and INT stated that they are not aware of any systematic fraud risk assessments in regional operations.

C. Control Activities

57. The policies and procedures that help ensure management directives are carried out. They help ensure that necessary actions are taken to address risks to achievement of the entity’s objectives. Control activities occur throughout the organization, at all levels and in all functions. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties.

58. These controls/processes and policies and procedures help ensure the Management directives are carried out. Control Activities occur throughout the organization, and include a range of activities. Thus, the ELCQ sought information on each of the activities noted above. Overall responses were positive concerning the Control Activities being carried out.

59. Operational practices followed and processes adequately documented. In assessing this part, Management reviewed the responses to the ELCQ; ROWs; the results of the 2005 and 2007 Staff Survey; the VR and Management’s Response to the VR.

(a) Overall, Respondents said, operational practices are being followed and processes have been adequately documented, and that Management and staff understand and follow the policies, written or practiced, as identified in various policies and manuals, including the Operational Manual, which contains Operational Policies (OPs) and Bank Procedures (BPs); the Administrative Manual; the Staff Manual; and various other manuals and guidelines. Although most Respondents to the ELCQ stated that the policies and procedures are clear and adequate, IAD noted that Bank-wide OPs/BPs need updating. IEG had stated in the Part IB Report that it believed out-dated OPs/BPs were a potential material weakness. OPCS has reviewed the process by which OP/BPs are updated, and management is of the view that the proposed IL reform will address most of the outstanding policy updates issues. Management, notes that as the main fiduciary policies (including OP/BP 12.00 on disbursements and 10.02 on FM) were issued in March 2007 and major instrument policies (including OP/BP 8.60 on DPLs and OP/BP 8.00, on emergency lending) are in place, this issue primarily affects OPs and BPs that apply to appraisal and supervision of IL. Based on management’s identification and mapping of the current process for policy revisions, management believes that the primary source for the current backlog in OP/BP updates is the micro style and approach to OP/BP drafting and content rather than the process for introducing policy changes that require OP/BP revisions. The principles-based approach to preparation of new OPs and BPs reflected in the more recent policy reforms, which focuses the OP and BP statements on core principles and key controls rather

37 These include: OP/BP 6.00 re expenditure eligibility, OP/BP 10.02 re financial management, OP/BP 12.00 re disbursement, OP/BP 13.20 re additional financing and OP/BP 8.00 re rapid response to crises and emergencies.
than detailed rules and procedures characteristic of the older statements, should help to minimize any future backlogs in OP/BP updates.

(b) Overall, however, there is some feeling that the policies and procedures are burdensome: for example, the ROWs highlight staff frustration with the burdensome nature of policies/procedures given the benefits. Further, staff feel that the cost/benefit ratio of controls over the administrative budget is very high. The staff’s perception is that (i) HRS and procurement have a knee jerk approach to controls rather than a service orientation; (ii) clearance requirements in operations are excessive, with too much review leading to delays in AAA and lending; and (iii) the costs imposed by multiple ex post review groups, such as, CSR, IEG, QAG, IAD, INT, and IP, are too high. Information gathered as part of the ROW exercises conducted by CTR provides valuable staff perspectives that complement more top-down work such as the Risk Scan. The fact that staff find policies burdensome and costs of controls exceeding the benefits is worrisome in its implications for the likelihood of compliance with Bank policies. Management needs to understand better whether this reflects a lack of understanding of the nature of controls. At the least, there is scope for better coordination across the control units.

(c) In the Part IB Report, QAG noted that policies and procedures concerning AAA would benefit from review and updating. Management is undertaking a broad review of the processes and controls, including systems and monitoring, that apply to AAA in order to simplify and strengthen them where needed, and ensure they are updated to take into account the wide variety of AAA currently carried out by the Bank. This review will also address the compliance weaknesses observed, along with other issues that have been raised by QAG in recent related reviews of AAA. Management expects to complete this review and discuss the recommended changes with the Board by late FY09.

(d) Finally, in its response to the ELCQ, INT expressed some concerns arising from its transaction-level investigations, especially as it refers to decentralized procurement.

60. **Management has clear objectives in terms of operating goals.** In assessing this part, Management reviewed the responses to the ELCQ; ROWs; the results of the 2005 and 2007 Staff Survey; the VR and Management’s Response to the VR.

- Respondents to the ELCQ said that, in general, appropriate indicators exist and are being monitored to (a) see if entity objectives are being met, (b) identify trends, and (c) prevent surprises. Some of this control activity and monitoring takes place through Quarterly Business Reviews (QBRs) and Key Performance Indicators (KPIs): for example, the KPIs in the Strategic Performance Contracts (SPCs) are linked to strategic objectives and

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38 There is a need for tighter oversight of AAA process (work in progress, slippages, delays in delivering policy notes, coding, reporting and dropped projects) by Regional and Network managers. There is also scope for OPCS, CSR, and ISG to work together with operations staff to resolve under lying problems for sustained systemic improvement.
operational goals for each business unit, including targets for KPIs. The KPIs are updated routinely. Some Respondents replied that, to strengthen the links to the institution’s mission, goals, and objectives for the current fiscal year the process would benefit from an institution wide validation of VPU-identified KPIs in terms of appropriateness and realism to institutional goals or priorities. Respondents also noted that no specific incentives are tied to the achievement of KPIs, and incentives for achieving goals in the organization are limited. Most Respondents noted, however, that Management expects the KPIs to be achieved in compliance with policies and procedures in an ethical manner. On the issue of meeting objectives and following through, INT expressed concerns about whether Management is learning and absorbing lessons, observing that some controls are being avoided at the transaction/project level.

61. **Duties are adequately segregated.** In assessing this part, Management reviewed the responses to the ELCQ; various IAD Reviews; the ICFR Results; and the COSO Report.

- Respondents generally agreed that duties are adequately segregated across the organization. Two Regions [EAP, LCR] pointed out that although segregation of duties is hard to achieve in small units, but they have identified the issue, and are monitoring it closely in their smaller units.

62. **Policies are in place to control access to computer programs and data files.** In assessing this part, Management reviewed the responses to the ELCQ; various IAD Reviews; the ICFR Results; and the COSO Report; and the Audit Committee Green Sheets.

- Policies are in place to control access to computer programs and data files. ISG continually monitors access, and IAD periodically conducts audits. IDA’s external auditor annually reviews controls related to IDA’s financial systems. Recently IAD identified that managers’ overriding of approval controls by sharing passwords had seriously affected access control effectiveness. In response, Management prepared an action plan, which has been discussed with both IAD and the AC, to strengthen the appropriate controls and prevent further overriding or intervention. The Part IB Report and other related ICFR work identified other deficiencies, and to address these deficiencies, Management has prepared action plans, discussed them with the external auditor, IAD and the AC, and is in the process of implementing the actions during FY08.

63. **Fraud and corruption.** In assessing this part, Management reviewed the responses to the ELCQ; various IAD Reviews; the COSO Report; INT’s Annual Report FY2007; the VR, and Management’s Response to the VR.

- Most units believe that IDA has implemented adequate controls in the areas associated with high risk of fraud and corruption, including through the annual COSO exercise, IAD work, and transaction-level controls in SAP. In the context of projects, reviews and arrangements established to address higher risks are seen as examples of dealing with fraud and corruption risks. QAG, however, noted that the risk of fraud is not assessed systematically in lending operations. IAD cited improvements underway in this area due to the GAC initiative and INT work. An MD [MDD] noted that there have been improvements in the past 12-24 months in the general strengthening of internal controls at regional levels in response to the GAC strategy and INT work. However the MD also believes that staff are still not well-informed about fraud and corruption indicators and how they can be brought to light. Finally, INT limited its response to controls in the context
of lending operations, and expressed a concern regarding the extent to which vulnerabilities to systemic fraud and corruption and/or INT’s findings are reflected in individual operations.

D. Monitoring

64. **Internal control systems need to be monitored** – a process that assesses the quality of the system’s performance over time. This is accomplished through ongoing monitoring activities, separate evaluations or a combination of the two. Ongoing monitoring occurs in the course of operations. It includes regular management and supervisory activities, and other actions personnel take in performing their duties. The scope and frequency of separate evaluations will depend primarily on an assessment of risks and the effectiveness of ongoing monitoring procedures. Internal control deficiencies should be reported upstream, with serious matters reported to top management and the board.

65. Monitoring controls/processes/activities assess the quality of IDA’s internal control system’s performance over time.

66. **Internal communications are effective in providing feedback to Management on whether controls are operating effectively.** In assessing this part, Management reviewed the responses to the ELCQ; QAG Reports (QEA, QSA, ARPP); IAD Audit Reports (e.g. Supervision Reporting Audit); IEG Reports; and IDA Internal Controls Part I findings.

- Numerous ongoing monitoring procedures are built in to the Bank’s normal, recurring operational activities. These ongoing procedures include operating reports; communications from external parties; an appropriate organizational structure and supervisory activities; data recorded by information systems compared with physical assets; and recommendations of the internal and external auditors. Overall internal communications are effective in providing feedback to Management on whether controls are operating effectively. These internal communications include feedback through the QBR process and through SPC, coupled with self-monitoring through CAS midterm reviews, mandatory annual project implementation status and results (ISR) reports, and implementation completion (ICR) reports at the conclusion of each operation. However, there is a need to review and improve the level of candor generally, and in the area of risk identification in particular, in project documents and monitoring reports (including PADs and ISRs). In this regard, one MD [MDD] noted that Staff in general may be reluctant to report problems, fearing that it reflects badly on their performance, while another respondent [INT] noted that it was aware of some cases of retaliation against staff for reporting problems.

67. **There are regular self-assessment exercises in the Bank.** In assessing this part, Management reviewed the responses to the ELCQ; QAG Reports (QEA, QSA, ARPP); ICFR; ROWs; Risk Scan; and IDA Internal Controls Part I findings.

- Annual self-assessment exercises review internal controls related to financial statements (ICFR), control environment (ROWs), entity level risks (Risk Scan), and the annual budget process. Operational staff also self-assess performance under all CAS’s and individual operations (including AAA activities) through completion reports. In addition, the Letter
of Representation that is signed by each Vice President brings an awareness of the issues being monitored.

68. **Management is responsive to internal and external recommendations.** In assessing this part, Management reviewed the responses to the ELCQ; QAG Action Plans; IAD quarterly reports to AC; IEG Management Action Records to CODE; the IP Annual Report, and the External Auditor’s Management Letter.

   (a) Processes and procedures are in place to monitor progress of actions agreed to remedy deficiencies identified, or to introduce needed improvements, in response to recommendations made through internal and external reviews and evaluations. Primary among these are: (i) QAG’s regular assessments of the quality of projects entering the portfolio and during supervision, including reviewing the procurement, financial management and safeguards aspects, and then provides recommendations to Management. These assessments are carried out at both project and portfolio levels; (ii) IAD’s annual audits/reviews of both financial and operational processes/activities, which set out recommendations for improvement to governance and internal controls; (iii) IEG’s program and project evaluations which focus on development effectiveness -- specifically whether programs and projects were able to achieve their development objectives; (iv) external auditor’s annual management letter which identifies internal control deficiencies arising during their audit of IDA’s financial statements and their review of ICFR, and (v) the Inspection Panel (IP) reviews and reports on complaints by potentially affected external parties related to Bank adherence to its operational policies in projects it supports.

   (b) QAG, IAD, IEG and the IP all follow evaluation standards of external organizations. These four units, together with the external auditor, have direct access to Senior Management and the Board. Their recommendations are closely monitored, and Management attempts to respond to the evaluators’ recommendations in a timely manner. However, some evaluators expressed concerns about actions taken by Management in response to their recommendations: for example, (a) IAD noted that Management ‘usually’ takes adequate and timely actions,39 and (b) IEG noted that the extent and timeliness of Management responses to their recommendations varies.

   (c) As stated above, processes and procedures are in place to monitor progress of agreed actions to remedy deficiencies, however, during the review it was noted that there is not a process, or unit, in the institution to consolidate all internal control related recommendations, irrespective of the evaluator/auditor, and to review such recommendations for (i) internal consistency; (ii) consistency in management’s responses; and (iii) identification of control related patterns.

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39 With respect to IAD itself, its quarterly update reports to the AC follow up on recommendations for audits rated unsatisfactory.
69. **Internal audit’s scope, responsibilities, and audit plans are appropriate for the organization.** In assessing this part, Management reviewed the responses to the ELCQ; IAD’s FY07 and FY08 Work Programs; and IAD’s TORs.

- IAD’s responsibilities are described in its Terms of Reference. The revised TOR has been sent to the President for his review and approval. In the meantime, IAD is using the Audit Committee’s TOR as a proxy. In addition IAD’s FY07 and FY08 work programs have been approved by the President and discussed with the Audit Committee.

70. **Internal audit adheres to professional standards, such as those issued by the Institute of Internal Auditors (IIA).** In assessing this part, Management reviewed the responses to the ELCQ; and IIA peer review report of IAD’s activities.

- IAD undergoes periodic peer review by the IIA, the last one of which was completed in FY06.

71. **Fraud and corruption.** In assessing this part, Management reviewed the responses to the ELCQ; INT’s Annual Report FY2007; and VR and Management’s Response to the Volcker Panel Report.

- With respect to fraud and corruption, INT expressed concerns in areas covering both “ongoing monitoring activities” and “separate evaluations”, stating that although INT is good at catching violations over the years, Management supervision has not increased materially in this timeframe.40

E. Information & Communication

72. Pertinent information must be identified, captured and communicated in a form and timeframe that enable people to carry out their responsibilities. Information systems (computerized, manual, or a combination) produce reports, containing operational, financial and compliance-related information that make it possible to run and control IDA’s business. They deal not only with internally generated data, but also information about external events, activities and conditions to inform business decision-making and external reporting. Effective communication also must occur in a broader sense, flowing down, across and up the institution. All personnel must: (i) receive a clear message from top management that control responsibilities must be taken seriously; (ii) understand their own role in the internal control system, as well as how individual activities relate to the work of others; and (iii) have a means of communicating significant information upstream. In addition, there needs to be effective communication with external parties such as shareholders, donors, borrowers, suppliers and regulators.

73. These controls/processes/activities help ensure the identification, capture and communication of pertinent information in a form and timeframe that enables staff and management to carry out their respective responsibilities.

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40 The example INT cited was that travel claim-related cases continue to show inadequate controls by reviewing managers.
1. Information

74. **Operational reporting and related applications and information systems are reliable.** In assessing this part, Management reviewed the responses to the ELCQ; the ICFR Questionnaire; the Business Warehouse; the QAG ARPP Report; the IEG ARDE Report; and the President’s brief to the Board.

(a) The Bank’s information systems are reliable. Management uses an array of information systems (both computerized and manual), which enable Management to (i) prepare accurate and timely operational reporting, (ii) obtain relevant information from external and internal sources for operational reporting systems, and (iii) have information available on a timely basis. Systems as Business Warehouse (BW), SAP, the Operations Portal, e-Consult, and e-Trust Funds produce reports containing the operational, financial, and compliance-related information that make it possible to run and control IDA’s business. In addition, the Board has access to the ED portal and an electronic distribution system that features full archival retrieval of a wide range of information. The Board also receives special briefings when they request further information from Senior Management or Regions on specific topics or operations.

(b) However, electronic information systems are sometimes inadequate to suit the needs of operational units that are decentralized. As with centralized units, the decentralized operational units are responsible for recording, collecting, analyzing, preparing reports and papers and distributing information to Senior Management and the Board. In these cases, much more manual intervention and accumulation of data is required in order to provide reliable and consistent aggregated reports to Senior Management and the Board.

(c) Broader than just the decentralized units, however, is the fact that it is often difficult to get consistent aggregated numbers (for example, on Bank-supported deliverables or budgetary allocations to specific priorities, information from all sources of funds). This difficulty may result from internal and external information gaps [MDD, AFR, ECA, FPD]. At times, obtaining necessary information requires manual intervention or merging reports for Bank Budget (BB) and Trust Funds (TF) and data manipulation, which may impair the integrity of the data being reported. One unit said there may be “too much information to digest,” and suggested “targeting reports to the type of VPU (Regions/Networks/FACs).” [FPD] As a result the above observations may point to an efficiency issue, although there are no obvious overlaps in the information provided, as they question whether so many units need to collect similar information. While another unit observed that SAP does not capture delivery of DEC products such as publications (e.g. working papers, special studies, journal articles, books, conferences). [DEC]

75. **Appropriate and necessary information is obtained from, and provided to, Management.** In assessing this part, Management reviewed the responses to the ELCQ; the ICFR Questionnaire; the Business Warehouse; ROWs; the QAG ARPP Report; the IEG ARDE Report; QBRs; 2005 and 2007 Staff Survey, and the President’s Brief to the Board.
Information capture for monitoring purposes occurs at the unit, corporate, and Board levels. At the VP-level, mechanisms include Regional portfolio and deliverables reports, while Senior Management-level reporting mechanisms include the Quarterly Business Review (QBR) and the President’s Brief. These reports provide periodic operational and budget information to Senior Management and may annex performance memoranda from individual VPU’s, providing more detailed information about VPU performance and internal/external issues, the execution of VPU work programs, and progress in meeting VPU objectives. External information is provided to Senior Management and operations units by EXT and by the Country Management Unit staff, and is also gathered for special purposes: for example, for activities related to Treasury’s asset management, Treasury’s performance system compares actual portfolio returns with pre-established benchmarks.

With respect to job functions, the recent Staff Surveys results showed that Staff felt they had adequate information to do their jobs (84% said yes in 2005; 82% said yes in 2007). Likewise, ROW results show Staff feel they can easily access such information.

Information is gathered from and disseminated to the appropriate people on a timely basis. In assessing this part, Management reviewed the responses to the ELCQ; the ICFR Questionnaire; the Business Warehouse; the QAG ARPP Report; the IEG ARDE Report; QBRs; and the President’s Brief to the Board.

Staff and managers, both in Washington and in decentralized offices, have appropriate access to financial and operational information in institutional systems such as SAP and BW. User satisfaction with systems varies across the institution, and some units/staff report more work is needed to improve the user-friendliness of systems [AFR, SAR, OPCS, QAG, HDN, SDN, LEG, WBI] and ease-of-access to reports, as well as to improve technology links to some decentralized offices.

The controls units review also noted that there could be improvements in the timeliness of the transfer of information.

There is a process for identifying and responding to the changing information and communication needs. In assessing this part, Management reviewed the responses to the ELCQ; the ICFR Questionnaire; QBRs; IPC (Information Policy Council) and ISC (Information Security Committee) TORs; and the President’s brief to the Board.

Management support for the development of necessary information systems is shown by the commitment of appropriate resources. The Board monitors resource priorities, including those related to information systems as part of the process of presenting to the Board of Governors an audit of accounts, and administrative budget, and an annual report on the Bank’s operations and policies as well as other matters at the Annual Meetings.

Identifying changing information and communication needs resides with the individual VPU’s. During FY07, a new governing committee, the Information
Policy Council (IPC), was established to ensure development or updates of information systems are based on a strategic plan linked to the overall strategy. The IPC includes members of Operations, Finance, Corporate, and Administration management teams. The fact that it is relatively new means that some business units may be either unaware or dissatisfied with the mechanism.41

(c) Changing client needs can be communicated through several channels, including feedback, comments, or complaints from external parties which are encouraged through consultations and during project preparation, as well as through CAS inputs from governments, civil society organizations, the private sector, NGOs, and donors.

78. **Business continuity.** In assessing this part, Management reviewed the responses to the ELCQ; the ICFR Questionnaire; QBRs; IPC (Information Policy Council) and ISC (Information Security Committee) TORs; and the President’s brief to the Board.

- Management has a policy for timely recovery of business functions, systems, processes and data captured in an institutional Business Continuity Plan (BCP) which mandates periodic testing and updates, and ISG performs such work according to policy, however, not all business units in HQ or in decentralized offices regularly test or update unit-level BCPs on a periodic basis.

2. **Communications**

79. **Management communicates staffs’ duties and control responsibilities in an effective manner.** In assessing this part, Management reviewed the responses to the ELCQ; HRS Job Descriptions; the Operations Manual; Procurement Policies and guidance; the FM Practices Manual; the Administrative Manual; Training Courses; ROWs; Kiosk announcements and desk-to-desk memos.

(a) Management has many tools in which various staff duties and responsibilities related to internal control are described, including, but not limited to: generic job descriptions (HRS and Business Units); operations manual (where BPs set out clearance responsibilities); procurement policies and guidance (where staff involved with operational procurement have responsibilities set out); FM practices manual (where FM staff have responsibilities set out); Administrative manual statements (which among other things sets out staff duties and responsibilities, including those for administrative expenses). However, issues have been identified including the lack of specific internal control responsibilities within the generic job descriptions by Business Units; delays in updating OPs/BPs which may mean that they do not necessarily reflect current process and responsibilities related to internal controls; adequacy of documentation relating to operations generally, including Procurement, during project

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41 Some of the dissatisfaction was reflected in the ELCQ responses of three units, who basically responded that “emerging information needs are flagged by different operational units of the Bank and not necessarily pursued/discussed in a systematized manner” [MDD, LEG, HRS]. In addition, two units reported that “specific needs of Country Offices, especially those resulting from increased decentralization, have not yet been fully met.” [AFR, EAP]
preparation/appraisal and supervision stages; and, lack of clear communication and information, including guidance, to support procurement work.

(b) Management uses the opportunities provided by bringing staff together in training sessions and self-assessments (ROWs and ICFR) to discuss staff responsibilities related to internal control and to obtain feedback and discuss instances of control failures. As noted above, in the 2005 Staff Survey 84% of Staff said they had adequate information to do their jobs, while 82% responded similarly in the 2007 Staff Survey.

(c) Management communicates with and updates staff via Kiosk announcements and desk-to-desk emails when new members of management are hired/appointed, units undergo major reorganization, changes are made to the systemic internal controls (e.g. the issue of password sharing), and control-related information is needed to be passed on throughout the organization (e.g. summary of INT findings).

80. **Channels of communication for staff to report suspected improprieties have been established.** In assessing this part, Management reviewed the responses to the ELCQ, and the Staff Manual.

- Multiple channels exist for reporting suspected improprieties, including: line management; the EBC and its Ethics Helpline for assistance with conflicts of interest or ethical dilemmas; Human Resource Officers (both in HRS and VPU); the Bank’s Conflict Resolution System (e.g., Ombuds Office, Mediation Services); INT; and the Staff Association. Staff are informed about the process for formal complaint of harassment, discrimination or other inappropriate behaviors in Staff Rule 8.01. There remains some confusion among staff regarding what to report and to whom, as well as concerns about the gap that exists in the absence of a revised whistleblower policy.42

81. **A "whistle-blowing" program has been established, and Management's reaction is monitored as it relates to operational matters.** In assessing this part, Management reviewed the responses to the ELCQ; ROWs; the Draft Whistleblower policy; the VR, and Management’s Response to the VR.

- The Bank has had whistleblower protections for some time. However, these require strengthening to provide staff with confidence that they can report alleged violations/improprieties without fear of retaliation. A revised whistleblower policy has been prepared by Management, reviewed with the Board’s Audit and Personnel Committees and is currently being circulated for public comment. Management will consider the feedback received from this final round of comment and proceed to obtain the necessary approvals for implementation of a new whistleblower policy as soon as possible.43 Responses to the ELCQ and anecdotal information from ROWs provide some

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42 INT expressed concerns about fear of retaliation and lack of reward to those who identify and report corruption. Since the submission of the ELCQ, the Board has adopted a strengthened Whistleblower Policy.

43 IAD has pointed out that the revised policy, in its view, falls short as it does not offer protection against reprisals for allegations of misconduct against Board members and the President. In June 2008, after the submission of the ELCQ, the Board adopted a strengthened Whistleblower Policy.
observations about Staff concerns: specifically, some Staff, particularly transaction processors and RM Staff, feared that they would be identified by their managers if they reported improper conduct and circumvention of controls. Other Respondents indicated concerns that not all responses to allegations have been investigated in a timely manner.44

82. **Management’s communication across and outside the organization reflects an attitude toward sound internal controls.** In assessing this part, Management reviewed the responses to the ELCQ; ROWs; the IBRD/IDA Annual Report; the 2005 and 2007 Staff Survey; and Kiosk announcements.

(a) Communication across the organization is adequate and the completeness and timeliness of information is sufficient to enable people to carry out responsibilities effectively. 2007 Staff survey results show that staff feel they have adequate information to do their jobs (82% said yes). ROW results also show Staff feel they can easily access such information. In addition, Management uses Kiosk announcements, broadcast e-mails, and other alerts to disseminate critical information throughout the Bank.

(b) The Bank has issued in its annual reports for IBRD and IDA and its financial statements and opinion on the adequacy of internal control over financial reporting, and it has disclosed the respective unqualified opinions of its external auditor. IDA’s assessment of its internal control over financial reporting is based on the most comprehensive practices.

(c) Communication with, and feedback from, external parties, including country office contact details are widely distributed. The external web is widely used by regions, and the network of Public Information Centers (PICs) acts as a public gateway and feedback mechanism for the Bank. Various systems are used to track key communications when received by the Bank, including, Encorr, Client Connections, e-Consult, the EXT network trust fund advisory committees, and partnership meetings. Timely and appropriate follow-up action by management to communications received from clients and other external parties.

(d) The mechanisms described above are used to ensure follow-up to such communication. In addition: (a) at the regional level, the EXT office is in charge of overall external communications and draws on the sectoral/CMU units as needed; and (b) at the country level, each country office has its own strategic communications strategy that aims to reach all key counterparts with the latest Bank information and updates on Bank business. Regions conduct routine operational procedures and outreach programs, regular consultation and dialogue with key stakeholders, especially civil society groups, including those critical of the Bank.

(e) As set out above, the Bank has recently amended the Principles of Staff Employment to enhance its current handling of whistle-blowing reports and claims of whistle-blowing retaliation. The new principle and staff rule puts the Bank Group at the leading edge of whistle-blowing protections amongst international organizations.

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44 EBC was uncertain whether managers or HR managers had taken appropriate follow-up actions in some cases.
consistent with the highest standards of good governance and the on-going efforts of the Bank to safeguard its integrity and effectiveness.

83. **Fraud and corruption.** In assessing this part, Management reviewed the responses to the ELCQ; INT’s FY2007 Annual Report; the VR and Management’s Response to the VR; and the ICFR Questionnaire.

- Most responders to the ELCQ agreed that IDA’s commitment to preventing fraud and corruption is clearly communicated to staff through the GAC papers, internal communications, as well as in annual COSO workshops. Sanctions reform, the existence of INT, and Volcker Panel Report were also cited as sources of heightened focus on this area. Most ELCQ Respondents believed that there was sufficient communication and increasingly more relevant training in this area. Additional information was also provided through the ICFR questionnaire related to increased emphasis, commencing in FY07, on online and in person ethics training made available through the Knowledge and Learning Board and EBC. However, an MD noted that evidence is lacking that practical knowledge in this area is widespread [MDD], and another unit has pointed out that as there is a need to raise awareness in this area (citing the Volcker Panel Report in support of its view) [LEG].

**F. Fraud and Corruption Controls**

84. Management observed that COSO added to its framework a component for reviewing fraud controls. This was added to specifically address the final rules adopted by the Securities and Exchange Commission (SEC), under the US Sarbanes-Oxley Act. Within this framework, fraud was defined in SAS 99 as:

“...an intentional act that results in a material misstatement in the financial statements that is the subject of an audit. Two types of misstatements are relevant to the auditor’s consideration of fraud – misstatements arising from fraudulent financial reporting, and misstatements arising from misappropriation of assets.”

85. Moreover, Management found that, as noted above, while Anti-fraud Programs and Controls are not currently a specific stand-alone component of COSO, in the IDA controls framework they are embedded in the other five components.

86. Consistent with the above, Management noted the Bank’s fraud risk assessment is performed, in conjunction with the internal control evaluation for financial reporting, at the entity and significant account/process levels. Furthermore, these individual risk assessments are performed based upon Management’s overall knowledge of controls in place, new activities, products and ventures, and historical fraud.

87. As noted previously (Fraud and Corruption section in “Methodology”), the ELCQ was the primary tool used by Management to assess fraud and corruption controls. Overall, responses to the ELCQ were positive, with a notable exception of INT’s responses. INT has responded to most questions from a transaction/project viewpoint rather than a
corporate/institutional perspective and has noted its concern with how fraud and corruption issues are addressed at the project level. Other units worth noting include: IAD, which placed a question mark and responded “unclear for the institution” on many of the questions posed; AFR, which responded “N/A” to many questions on the basis of the current content of its regional risk scan, which does not specifically cover fraud and corruption issues; IEG, which also responded “N/A” to majority of questions given that it has not evaluated the areas being covered; and HR which gave little substantiation for its responses.

88. The two questions to which several units responded in the negative include: (i) the effectiveness IDA’s whistleblower programs (Q8), and (ii) whether the fraud risk assessment is performed in a systemic manner (Q18). On the effectiveness of the whistleblower program, MDD, CFO, CSR, IAD, EXT and LEG have pointed to the need to adopt a new whistleblower policy to clarify and strengthen the protections to staff against reprisals. On the systemic fraud risk assessment, CFO, CSR, and QAG have suggested that while much is done to identify, assess and mitigate fraud risk at the transaction and corporate levels, the existing assessment tools need to be strengthened to ensure a more systemic approach to the fraud issue. INT, IAD and IEG have replied “N/A” for different reasons: INT has noted that it launches investigations after it receives allegations and is unaware of any “systematic” fraud risk assessments in regional operations; IAD responded with a question mark and commented that it is “unclear for the institution”; and IEG explained that it has not evaluated the IDA’s fraud risk assessment activities.

1. Control Environment relating to Fraud and Corruption Issues

89. Questions in this area focused on mechanisms in place to report and follow-up on allegations of fraud and corruption. Overall, most units opined that IDA has good communication channels/mechanisms in place for reporting fraud and corruption matters to appropriate/responsible parts of the Bank (primarily INT) through hotline, staff/manager communications, and through various channels that fall under the Conflict Resolution System. Staff Rule 8.01 was also cited as an important source for clarifying staff responsibilities and options on what to report to whom in the area of fraud and corruption. Some concerns were expressed regarding a gap that exists in the absence of a revised whistle-blower policy (LEG, EXT, CSR, CFO, MDD, IAD), which would hopefully be addressed under the new policy (a draft is posted on the Bank’s external web-cite with comments sought by February 22, 2008).45 Some concerns were also expressed regarding remaining confusion among some staff on what to report to whom and worries about potential reprisals. Questions were also raised regarding lack of information on follow-up actions due to confidentiality issues, which undermines staff confidence in effectiveness of the system.

2. Fraud Risk Assessment

90. Most responders agreed that IDA considers potential for fraud and corruption as part of its enterprise-wide risk-scan, with COSO, IAD audits, and unit-specific risk scan exercises cited most frequently as the primary tools. Most responders also believe that we have effective unit-level controls in the fraud and corruption (F&C) area, with the following control sources/tools cited in support of this view: (i) unit-level controls put in place by the Resource Management

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45 In June 2008, after the submission of the ELCQ, the Board adopted a strengthened Whistleblower Policy.
(RM) teams; (ii) controls embedded in SAP; (iii) institution-wide initiatives and assessments (including Risk and Opportunity Workshops (ROW), COSO Workshops, the Quarterly Business Reviews (QBRs), Risk Scan Exercises, Letters of Representation (LOR)); (iv) IAD audits; (v) external auditors; and (vi) the ongoing Quality Assurance Reviews conducted by ACT. There was some disagreement, however, on whether a fraud risk assessment is performed in a systematic way. While most responders believe that such assessments are indeed performed in a systematic way, CSR, CFO and QAG have responded “no” to this question. In support of this answer, they pointed out that while much is being done to identify, assess and mitigate fraud risk at the transaction and corporate levels (with CSR noting that fraud risk assessments are embedded in the overall risk assessment processes), the existing assessment tools need to be strengthened to ensure a more systemic approach to the fraud issue. INT has stated that from transaction-level perspective, they are not aware of any systemic fraud risk assessments in regional operations. IAD also noted that it is “unclear” on whether a systemic fraud risk assessment is conducted at the institutional level though it confirmed that fraud risk assessments form part of its annual risk assessment. (HR answered several questions in this area in the negative but cross referenced its reasons to an earlier question, which it has answered in the positive, so this was treated as a transcription error).

3. Control Activities

91. Most units believe that IDA has indeed implemented adequate controls in the areas associated with high fraud and corruption risk, including through the annual COSO exercise, IAD work, and transaction-level controls in SAP. In the context of projects, reviews and arrangements established to address higher risks are seen as examples of dealing appropriate with fraud and corruption risks. IAD cites improvements underway in this area due to the GAC initiative and INT work. INT limited its response to controls in the context of lending operations, and stated that based on its findings it believes that IDA does not adequately address the vulnerabilities in its lending programs in countries with systemic corruption and still does not make real-time adjustments to project implementation based on INT findings. QAG has noted that the risk of fraud is not assessed systematically in lending operations. MDD also responded that while there have been improvements in the past 12-24 months in general strengthening of internal controls at regional levels in response to the GAC strategy and INT work, staff are still not well-informed about the fraud and corruption indicators and how they can be brought to light.

4. Information and Communication

92. Most responders agreed that IDA’s commitment to preventing fraud and corruption is clearly communicated to staff through the GAC papers, internal communications, as well as in annual COSO workshops. Sanctions reform, the existence of INT, and Volcker Panel Report were also cited as sources of heightened focus on this area. Most also believe that there is sufficient communication and increasingly more relevant training in this area. Additional information was also provided through the ICFR questionnaires related to increased emphasis commencing in FY07 on online and in person ethics training made available through the Knowledge and Learning Board and EBC. MDD noted that evidence is lacking that practical knowledge in this area is widespread and LEG has pointed out that as there is a need to raise awareness in this area (citing the Volcker Panel Report in support of this view).
Annex A: Attachment: Board’s Role, Procedures and Decision-Making

93. This Memorandum\(^1\) describes the role of the Board in the control system of the International Development Association (IDA) as part of an overall review of internal controls over IDA operations. As consistent with the terms of reference for the review, this memorandum sets out the primary control functions of IDA’s Executive Directors within the context of its legal framework and current practice. It also examines the main documentation, processes and tools available to the Board in its decision-making. Lastly it describes the recently revised Code of Conduct for Board Officials and Ethics Committee procedures.

A. The Board’s Primary Control Functions—the Legal Framework

94. IDA’s Articles of Agreement (the Articles) provide that “[t]he Association shall have a Board of Governors, Executive Directors, a President and such other officers and staff to perform such duties as the Association may determine.”\(^2\) The Articles also vest all powers of the Association in the Board of Governors and permit the Board of Governors to delegate its powers to the Executive Directors except those specifically reserved to the Governors.\(^3\) The Board of Governors delegated its non-reserved powers to the Executive Directors, while limiting the Executive Directors from taking any action pursuant to that delegation “which is inconsistent with any action taken by the Board of Governors.”\(^4\)

95. The basic provisions of the Articles on the role of the Executive Directors read as follows:

“The Executive Directors shall be responsible for the conduct of the general operations of the Association, and for this purpose, shall exercise all the powers given to them by this Agreement or delegated to them by the Board of Governors.”\(^5\)

96. Furthermore, the Articles require that “[the Executive Directors] shall meet as often as the business of the Association may require.”\(^6\)

97. The Articles also contain provisions regarding the relationship between the Executive Directors and the President:

“The President of the Bank shall be *ex officio* President of the Association. The President shall be the Chairman of the Executive Directors of the Association but shall have no vote except a deciding vote in case of an equal division. […] The President shall be chief of the operating staff of the Association. Under the direction of the Executive Directors he shall conduct the ordinary business of

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\(^2\) Article VI, Section 1.

\(^3\) Article VI, Section 2(a) and (c).

\(^4\) By-Laws, Section 5.

\(^5\) Article VI, Section 4(a).

\(^6\) Article VI, Section 4(f).
the Association and under their general control shall be responsible for the organization, appointment and dismissal of the officers and staff."7

98. **History.** The above-quoted provisions of the IDA Articles are similar to those of the International Bank for Reconstruction and Development (the Bank). A brief examination of the latter’s drafting history can help shed little light on how Board/Management relations have evolved in the two agencies. The drafting history of the provisions of the Bank’s Articles related to the Executive Directors and the President is very sparse. At the Bretton Woods Conference, the relevant provisions of the Articles of Agreement of the International Monetary Fund (IMF) were discussed first and very little time was left to discuss the provisions of the Bank’s Articles. The provisions of the original IMF Articles were incorporated in the Bank Articles with few changes.

99. The Bank’s first President, Eugene Meyer, took office in June 1946. He resigned in December of the same year. Among the reasons for his departure, the frustration of being a person with responsibility but no authority has been highlighted.8 His successor, Mr. McCloy, accepted the post only after an understanding was reached with the Executive Directors as to their working relationship. This was embodied in the June 4, 1947 “Memorandum with Regard to Organization and Loan Procedure” (the 1947 Memorandum). The 1947 Memorandum was revised through 1956 on points of detail, but paragraphs 1 and 2, which establish the basic understanding of the relationship between the Executive Directors and the President, have remained unchanged. The arrangements provide:

“1. The Executive Directors are responsible for the decision of all matters of policy in connection with the operations of the Bank, including the approval of loans.”

“2. The management is responsible for developing recommendations on all matters of policy requiring decision by the Executive Directors. Whenever, in connection with the operations of the Bank [and the Association], decision of a question of policy becomes necessary, the President will submit such question to the Executive Directors with the recommendation of the management as to the action to be taken.”9

The same arrangements have been followed for IDA, including Board approval of IDA financing (credits, IDA grants and guarantees).

**B. Board control functions—documentation, processes and instruments**

100. Within the broad legal and historical context outlined above, this section discusses more specifically the various Board functions, as well as the processes and instruments available to the Board in carrying out those functions. A summary of the main Board decisions in Table format is also provided in Annex 1 for ease of reference.

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7 Article VI, Section 5(a) and (b).
1. Operational policy, strategy and instruments

101. Policy and sector papers. In accordance with the 1947 Memorandum, the Executive Directors are responsible for decisions on policy matters, while the Management is responsible for preparation and submission of recommendations to them. Thus, where a policy paper or a sector paper presents a new policy for the Association or a change in previously approved policy, the Board’s approval of the policy or policy change is required. The Management is responsible for the implementation of the Association’s policy.

102. Various Board committees on Board procedures have, over time, commented upon the format of policy papers considered by the Board. Most recently, the Board Effectiveness paper provided that all Board policy papers should (i) contain a two-page Memorandum of the President or Executive Summary identifying all key issues to be addressed by the Board; (ii) present options and reasons for recommendations or conclusions; (iii) outline previous decisions and the relevant legal background; and (iv) set out cost implications. Earlier, the Toure Report had emphasized that policy papers should be concise and focused and include “a clear statement of the Management’s recommendations and the reasons for these.” The Board, in adopting the Toure Report, followed previous Boards in reconfirming the use of a “chairman’s summing-up” for policy and sector discussions. When the chairman’s summing up was introduced in 1988, it was intended “to be used by the Executive Directors to inform their authorities and by the staff for guidance on policy matters.”

103. Sector policy reviews were recommended by the Naim Report, to take stock of experience and provide new policy directions where needed. In 1995, the Board accepted the recommendation of the 1995 Review and adopted Management’s proposal for a standard five year period between formal sector reviews. Currently, Sector Strategy Papers (SSP) are considered by the Board, and where sector policies or policy changes are proposed, the Board’s approval of the policy content of the paper or any policy change is requested, based on Management’s recommendations. In addition, Management prepares periodic reviews of sector strategy implementation, which are consolidated in the annual Sector Strategy Implementation Update (SSIU) for the information of the Executive Directors.

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12 Id. at paragraph 50.
14 “Report of the Ad Hoc Committee on Board Procedures,” as approved by the Executive Directors on August 4, 1992, incorporating R92-103; R92-103/1; R92-103/2 [Naim Report], paragraph 53 (c).
16 See also, “Enhancing the Board’s Focus on Implementation and Results on the Ground,” R97-5, January 14, 1997, paragraph 2. The Bank’s Disclosure Policy provides that the Chairman’s Concluding Remarks on a Sector Strategy Paper (SSP) are publicly available, unless the Executive Directors decide otherwise, while the Chairman’s Concluding Remarks on other policy and strategy issues may be made publicly available by decision of the Executive Directors. “World Bank Policy on Disclosure of Information,” September 2002 [Disclosure Policy], paragraphs 14 and 66. For SSPs, the summary issued is more frequently referred to as the Chairman’s Summing-Up.
104. **Operational policies.** In the implementation of the World Bank’s operational policies, Management currently issues two types of documents: Operational Policy (OP) statements and statements of Bank Procedure (BP). These apply to both Bank and IDA operations unless otherwise stated. OP statements, as well as Management’s proposed amendments and deviations from them, should be consistent with the Association’s Articles of Agreement, as interpreted by the Board, and with Board-approved policies. Deviations from Board-approved policy content are brought to the Board for consideration.\(^\text{17}\)

105. **Country Assistance Strategy (CAS).** The CAS for a particular country describes the Bank Group’s strategy based on an assessment of the country’s own strategies and priorities, and indicates the level and composition of assistance to be provided based on the strategy and country’s portfolio performance. The CAS is the result of discussions between Management and the country’s authorities, but it is not a commitment on the part of the Bank Group or the country to a specific lending program.

106. The Executive Directors discuss the CAS, but do not approve, reject or endorse this presentation of the Management’s strategy for lending and other activities to support the particular member country.\(^\text{18}\) Management is expected to take into account the views expressed by Board members, as summarized by the Chairman in the Concluding Remarks, in developing a country’s lending program and in the formulation of future CAS.\(^\text{19}\)

107. The specific operations for that country are presented to the Executive Directors for approval, as described in paragraphs 16-20 below. Where an operation deviates significantly from the agreed CAS framework, the Memorandum of the President (or President’s Report) should explain why.\(^\text{20}\)

108. **Poverty Reduction Strategy Paper (PRSP) and Joint IDA-IMF Staff Advisory Note (JSAN).** PRSPs, introduced in 1999 for IDA countries,\(^\text{21}\) describe a country’s macroeconomic, structural and social policies and programs to promote growth and reduce poverty, as well as associated external financing needs. PRSPs are country-driven and provide the basis for assistance from the Bank/IDA and the IMF, as well as debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative.\(^\text{22}\) PRSPs and PRSP progress reports are country-owned documents, and are not approved by the Executive Directors.\(^\text{23}\) The accompanying JSAN provides the staffs’ views of the country’s strategy to promote growth and reduce poverty, and provides the staffs’ advice on key priorities for strengthening the strategy and promoting its effective implementation. Directors are asked whether they agree with the staffs’ conclusions on (a) areas in which further analysis or adjustments are needed, (b) measures for improving PRS

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\(^{18}\) The Chairman’s Concluding Remarks for a Country Assistance Strategy (CAS) discussion are publicly available except when the CAS itself is not disclosed. Disclosure Policy, supra note 16, paragraph 9.

\(^{19}\) 1995 Review, supra note 15, paragraphs 11-12.

\(^{20}\) Bank Procedures (BP) 2.11, Country Assistance Strategies, paragraph 14. Such a project is not eligible for presentation under streamlined procedures. For discussion on streamlined procedures, see paragraph 19 below.

\(^{21}\) The discussion here of Poverty Reduction Strategy Papers (PRSPs) also includes Interim PRSPs (known as I-PRSPs).

\(^{22}\) Countries seeking assistance under the HIPC Initiative should have a PRSP or I-PRSP in place. “Poverty Reduction Strategy Papers: Operational Issues,” R99-241, December 10, 1999 [PRSP Paper], paragraph 51.

\(^{23}\) Chairman’s Summing Up of December 20, 1999 discussion of the PRSP Paper, supra note 23, recorded in Minutes of Meeting on December 20, 1999, M99 68, IDA/M99 67, January 5, 2000.
implementation, (c) implementation risks and measures to address them, especially the risks relating to debt-sustainability.24

109. **Operations (credits, guarantees, and IDA grants).**25 The Articles authorize the Association to “provide financing to further development in the less-developed areas of the world” subject to conditions set out in the Articles.26 These conditions include, among others that (i) except in special circumstances, financing be for specific projects; (ii) alternative financing at reasonable terms be not available to the borrower from private sources; and (iii) proceeds from financing be used “only for the purposes for which the financing was provided, with due attention to considerations of economy, efficiency and competitive international trade and without regard to political or other non-economic influences or considerations.”27

110. The Articles state that financing by the Association shall take the form of loans, unless the funding is specifically authorized for other types of financing, such as grants and guarantees. The Articles do not specify which organ exercises the power to make loans. Since the Association’s inception, approval of loans has been deemed as part of the function of the Executive Directors28 as consistent with the 1947 Memorandum. IDA financings are presented to the Executive Directors for approval at formal meetings.29

111. The Executive Directors have authorized the delegation of loan approval authority to the President only in very limited circumstances.30 Since 1975, the Executive Directors have delegated to the President the authority to approve advances from the Project Preparation Facility,31 through a tacit interpretation of the Articles.32 In 1997, the Executive Directors further delegated loan approval authority to the President in connection with the introduction of Learning and Innovation Loans (LILs) and Adaptable Program Loans (APLs). LILs are loans of $5 million or less financing small, experimental, risky and/or time-sensitive projects in order to pilot promising initiatives or experiment with an approach prior to larger-scale interventions. APLs are used in a series of loans to provide phased support for an agreed phased long-term development program. The President was authorized to approve LILs, subject to a seven-day

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24 The Chairman’s Summing-Up of such a PRSP discussion is publicly available. Disclosure Policy, supra note 16, paragraph 12.
25 “Operations” as used here includes IDA financing, whether in the form of credits or, where authorized, on a grant basis. This includes IDA 13 Grants, as well as HIPC and Post Conflict Grants made under the authority of earlier replenishments. For a discussion of IDA’s grant-making authorities, see “IDA Grants to Countries in Arrears,” Ko-Yung Tung, April 2, 2002, in Selected Legal Advice of the General Counsel 1999-2002, OM2002-0123, December 11, 2002, [Selected Legal Advice] at page 125.
26 Article V, Section 1.
27 Article V, Section 1 (b), (c) and (g).
29 See paragraph 30 below.
30 The President has further delegated that authority to the Regional Vice Presidents (RVPs).
31 “Assistance in Project Preparation,” R75-224, November 17, 1975, approved by the Executive Directors December 16, 1975 (M75-52, December 22, 1975). Advances from the Project Preparation Facility are refinanced as part of the subsequent loan, or, if there is no loan, repaid over a fixed period. OP 8.10, “Project Preparation Facility,” February 2002, paragraphs 5-8.
period for Executive Directors to pose questions and provide comments.\textsuperscript{33} For APLs, the first APL for a program would be approved by the Executive Directors under the streamlined procedure if no significant issues are involved.\textsuperscript{34} The President is authorized to approve follow-on APLs in principle, subject to a ten-day period for Executive Directors to request a Board discussion.\textsuperscript{35} If at least three Executive Directors request a meeting to discuss such a follow-on APL, the loan is scheduled for Board consideration and approval; otherwise, Management’s approval takes effect at the end of the ten-day period. In practice, Board discussion of follow-on APLs has been requested and taken place.

112. Procedures have been in use since 1973 for Board consideration of more routine operations without discussion by the Executive Directors\textsuperscript{36} to allow the Board to spend more time discussing general policies and assistance strategies for individual countries. These “streamlined procedures” were further revised in 1992 and, more recently, in 2005, when the Board Effectiveness paper introduced streamlining of first phase APLs raising no policy, fiduciary or operational issues.\textsuperscript{37} It is expected, however, that at least one operation for a country will be considered under regular procedures within about a year of its CAS discussion, even if all operations meet these criteria for streamlined procedures. When an operation has been scheduled for consideration under streamlined procedures, Executive Directors may nevertheless request a general discussion or raise an issue at the meeting by giving three days’ advance notice to the Corporate Secretariat.\textsuperscript{38}

113. Guarantees are presented to the Executive Directors for approval under regular procedure rather than streamlined procedures.\textsuperscript{39} The Board approves the parameters and terms and conditions under which a guarantee may be given by the Association, normally before negotiations have been completed. Consequently, if the negotiations result in any substantial changes in the terms of the guarantee from those approved by the Board, the guarantee is resubmitted for Board approval of the changes.\textsuperscript{40} Thus far, no guarantees have required resubmission for Board approval after negotiations.

\textsuperscript{33} Adaptable Lending Paper, supra note 32, paragraphs 44-48, 97 and 108. The Paper specified, in paragraph 48, that the President’s authority would be exercised by the RVPs, under the oversight of the Managing Director for Operations.

\textsuperscript{34} Board Effectiveness Paper, supra note 10, paragraph 64.

\textsuperscript{35} Adaptable Lending Paper, supra note 32, paragraphs 72, 97 and 108, as amended. Minutes of Meeting of Executive Directors on September 4, 1997, M97-56, IDA/M97-55, September 26, 1997, paragraph 3(i) (a) and (b). The Paper also specified, in paragraph 72, that the President’s authority would be exercised by the RVPs, under the oversight of the Managing Director for Operations.

\textsuperscript{36} The “special procedure” for approving routine lending operations was introduced in 1973. “Review of Board Procedures,” R73-225, September 13, 1973, as approved by the Executive Directors in Executive Session on October 16, 1973 (XM73-2/1, October 25, 1973, paragraph 4(e)). This was revised to the “streamlined procedure” in 1992. See Naim Report, supra note 14, paragraph 31.

\textsuperscript{37} Board Effectiveness Paper, supra note 10, paragraph 64.

\textsuperscript{38} “Implementation of the Report of the Ad Hoc Committee on Board Procedures,” R92-178, October 7, 1992, approved by the Executive Directors on October 20, 1992 (M92-72, November 10, 1992) [Implementation Memorandum], paragraph 8; BP 10.00, Annex K, paragraph 2.


\textsuperscript{40} BP 14.25, paragraph 24. In such a case, signing of the legal documents would take place after final Board approval.
114. **Partnerships.** The Articles do not specifically refer to the responsibility for IDA’s partnerships with other entities. The Articles do, however, require Board of Governors’ approval for some IDA partnerships. Certain types of cooperation with other international organizations fall within the Board of Governors’ non-delegable power to “make arrangements to cooperate with other international organizations (other than informal arrangements of a temporary and administrative character).”\(^{41}\) IDA practice has been that Board of Governors’ approval has been sought for cooperation arrangements between the Association and other public international organizations that are formal in nature, general in scope, and indefinite in duration.\(^{42}\) Board of Governors’ approval has not been required for arrangements with public international organizations whose primary purpose is not cooperation, that are informal or ad hoc, that are for a limited duration, or that are administrative, as opposed to institutional or operational in character.\(^{43}\)

115. Many other aspects of partnerships fall outside these reserved powers. Executive Directors approve the policy framework for the engagement of the Association in partnerships, while Management has the responsibility for approving individual partnership arrangements, based on the criteria contained in this policy framework. Executive Directors’ approval is also needed in those cases where the President proposes to serve as a director of an entity established in respect of activities resulting from the partnership.

116. **Trust Funds.** IDA often acts as administrator or trustee of trust funds, with funds from bilateral, multilateral and other donors. In administering such trust funds, IDA must be guided by its purposes as set out in the Articles.\(^{44}\)

117. Approval of IDA administration of trust funds has been sought from the Executive Directors where the trust fund is funded by transfers from the Bank’s net income or surplus, in conjunction with the Bank process for the approval from the Bank’s Board of Governors of the allocation of income or surplus. Executive Directors’ approval is also required where the trust fund would provide assistance for entities not included in the IDA membership.\(^{45}\) Finally, where a trust fund presents novel or significant issues. Management has also sought the approval of the Executive Directors.

118. **Grants.**\(^{46}\) IDA financing on a grant basis (such as IDA 13 and 14 Grants, IDA Post Conflict Grants and IDA HIPC Grants) requires Board approval, as outlined in paragraph 17 above. Grants from IDA-administered trust funds are not IDA’s own financing and do not require Board approval unless the trust fund documents specify otherwise.

\(^{41}\) Article VI, Section 2 (c) (v).

\(^{42}\) “Legal Note on Cooperative Arrangements with Other International Organizations,” Vice President and General Counsel, February 12, 2001, paragraph 4, in Selected Legal Advice, supra note 25, at page 27. The Legal Note also provides illustrations of cooperative arrangements that were sent to the Bank Governors for approval.

\(^{43}\) Id.


\(^{45}\) The determination that IDA administration of a trust fund benefiting territories outside its membership benefits the members as a whole has been requested from the Executive Directors, who, as per Article X(a), have the power to interpret the Articles of Agreement.

119. **Monitoring and Evaluation.** The Board has broad oversight on whether IDA’s operational results are met. The **Independent Evaluation Group** (IEG) is an independent unit within the World Bank Group, which reports directly to the Boards of the Bank and IDA.\(^{47}\) Under the oversight of the Board Committee on Development Effectiveness (CODE),\(^{48}\) IEG is headed by a Director General, Evaluation (DGO), who is appointed by the Board for a renewable five-year term. IEG independently evaluates IDA strategies, programs, projects and corporate activities with a view to identifying the contribution of the Association to a country's overall development. The goals of evaluation are to learn from experience, to provide an objective basis for assessing the results of the Association's work, and to provide accountability in the achievement of its objectives. It also improves the Association’s work by identifying and disseminating the lessons learned from experience and by framing recommendations drawn from evaluation findings. IEG’s programs and budget are reviewed by CODE and approved by the Executive Directors. IEG evaluation findings are reported directly to the Board and shared with the public under Board-approved disclosure policies.

120. **Inspection Panel.** Operational policies aim at ensuring effectiveness, but also transparency and fairness as the Bank and IDA carry out their work. On September 22, 1993, Executive Directors of the IBRD and IDA established the **Inspection Panel**\(^{49}\) with the primary purpose of addressing the concerns of the people who may be affected by World Bank’s projects and to ensure that the Bank and the Association adhere to their operational policies and procedures during the design, preparation and implementation phases of projects. The Inspection Panel reports directly to the Board and consists of three members who are appointed by the Board for non-renewable periods of five years. Members are selected on the basis of their ability to deal thoroughly and fairly with the requests brought to them, their integrity and independence from the bank Management, and their exposure to developmental issues and living conditions in developing countries.

121. The Panel can receive requests for inspection by an affected party in the territory of the borrower which is not a single individual, or by a representative of such party, whose rights or interests have been or are likely to be directly and materially affected as a result of a failure of IDA to follow its operational policies. In view of the institutional responsibilities of Executive Directors in the observance by IDA of its operational policies and procedures, an Executive Director may in special cases of serious alleged violations of such policies and procedures ask the Panel for an investigation. The Executive Directors, acting as a Board, may at any time instruct the Panel to conduct an investigation.

122. Before a request for inspection is heard, the Panel satisfies itself that the alleged violation is of a serious character and that Management, having dealt with the subject matter of the request, has failed to demonstrate that it has followed, or is taking adequate steps to follow policies and procedures. The Panel’s report on an inspection considers all relevant facts, and concludes with the Panel’s findings on whether IDA has complied with all relevant policies and

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\(^{48}\) Id. See also “Standing Committees,” Resolution Nos. 06-0010, IDA 06-0007, IFC 06-0067, October 20, 2006 [Standing Committee Resolution], paragraph 3(a).

ANNEX A: ENTITY LEVEL CONTROLS

procedures. In response to the Panel’s findings, Management submits to the Executive Directors for their consideration a report indicating its recommendations within six weeks from receiving the Panel’s findings. All decisions of the Panel on procedural matters, its recommendations to the Executive Directors on whether to proceed with the investigation of a request, and its reports, are reached by consensus and, in the absence of a consensus, the majority and minority views are stated. Both the request for Inspection and the Inspection Panel Report and management response are made publicly available after consideration by the Executive Directors. An annual report on the Panel’s activities is also provided to the Executive Directors and published.

123. **Disclosure.** Under its 2002 information disclosure policy, IDA makes a considerable amount of operational information available to the public, ranging from project and policy documents to strategy and evaluation documents. On March 8, 2005, the Board approved a number of revisions to the policy on the disclosure of information. The 2005 policy revisions aimed at improving and enhancing the Bank’s record on information disclosure. These changes reaffirm the commitment of the Bank and IDA to ensuring increased transparency about their activities. Notably, the 2005 revisions included a provision for disclosure of Board minutes.

2. **Finance and administration**

124. **Financial Statements.** Executive Directors review and approve the Association’s financial statements. As per Article VI Section 11, the Association publishes a report containing an audited statement of its accounts annually and circulates summary statements of its financial position to members at intervals of three months or less.

125. **Net Income.** The Articles provide that the Board of Governors determines from time to time the disposition of the Association’s net income, if any. To date, no such disposition has been made.

126. **Risk Management.** A new framework for provisioning against probable losses in IDA’s portfolio of development credits and guarantees, a requirement under US GAAP, has been approved by the Board on December 11, 2007. The new framework is based on the IBRD’s LLP framework, while reflecting IDA’s specific financial structure and portfolio characteristics including the concessional nature of IDA’s lending activities.

127. **Strategic Planning and Administrative Budget.** Every year, Management prepares a Medium-Term Strategy and Finance (MTSF) paper, which presents the Executive Directors with an integrated picture of the World Bank’s strategic priorities, income and expenditure, including a comprehensive overview of IDA’s financial outlook. The MTSF draws from extensive management discussions as well as consultations on these matters between management and the Board. The review of the MTSF precedes, and provides a context to, the annual approval of the World Bank’s administrative budget by the Executive Directors.

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50 Disclosure Policy, supra note 16.
52 Article VI, Section 12.
128. **Managerial Appointments.** The appointment of the Bank’s officers and staff is among the direct responsibilities of the President, subject to the general control of the Board. The “general control” to be exercised by the Executive Directors related to staff appointments has customarily been confined to advance notice of proposed senior level staff appointments. The practice of informal discussion of proposed senior level staff appointments was first formalized in 1973 when the President and the Executive Directors agreed that the President would send the qualifications of proposed senior management appointees to the Executive Directors for comment five days in advance of appointment (for Department Directors, the period was 24 hours). During the advance period, the President proposed that:

> “any Executive Director may provide me with comments he may wish to make regarding the appointment or extension. Should any Executive Director so desire, I will convene an executive session of the Board to discuss the matter before taking any further action.”

129. These practices have remained in place, with modifications in positions covered and timing approved by the Executive Directors in 1999. The current, modified procedure requires that Management provide three working days’ advance notice to the Board of (a) appointment to all managerial positions graded GI and above, regardless of title; (b) appointment of all Country Directors, regardless of grade; and (c) reassignment of any manager graded GI and above or of any Country Director to a newly created position or to a position of Vice President or above.

130. Certain senior positions require greater involvement by the Board. The Director-General, Evaluation (head of the Independent Evaluation Group), the members of the IBRD/IDA Inspection Panel and the judges of the World Bank Group Administrative Tribunal are each appointed by the Board on the nomination of the President. While the Auditor General, Group General Counsel and Corporate Secretary are all staff positions, appointed by the President, provision has been made for Board involvement in the appointment process (exercised by the Audit Committee in the case of the Auditor General).

### 3. Board procedures and instruments

131. Board procedures and decision-making have evolved over time as the Executive Directors and Management have agreed on the applicable rules. The rules and practices have been continually revised and updated, generally through the mechanism of a Board review of procedures. The most recent review was a 2005 Report entitled *Board Effectiveness: Making Board Decision-making Processes More Efficient (Board Effectiveness).* Previous reviews include the 2000

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54 IDA Article VI, Section 5 (b). In practice, IBRD officers generally serve in the same capacity for IDA.
58 These arrangements are described in paragraphs 9-14 of the 2007 Legal Memorandum, *supra* note 55.

132. The Executive Directors conduct their business in several different formats, depending on the matter under consideration and the action to be taken. The Executive Directors meet in both formal and informal meetings. Technical briefings are held for Executive Directors and those in their offices. The Executive Directors also meet as the Committee of the Whole, in the Steering Committee and in Board Committees. These formats are described below.

133. Under the Articles,\textsuperscript{64} the President serves as Chairman of the Board for all meetings of the Board. Under the Board’s Rules of Procedure for meetings, a Managing Director designated by the President acts as Chairman in his absence.\textsuperscript{65} However, when a meeting is convened to consider the President’s appointment or terms and conditions of service, or “under such other exceptional circumstances in which the President shall have determined that it would be ‘inappropriate’ either for him or for a Managing Director to act as Chairman, an Executive Director selected by the Executive Directors acts as Chairman.\textsuperscript{66}

134. **Formal Meetings.** Where the Executive Directors are called upon to take decisions for the Association, a formal meeting of the Board is the appropriate forum. For routine operational and administrative decisions, approval is sought without meeting, i.e., by circulation of a proposal on a no objection basis.

135. Items submitted for approval on an absence-of-objection (AOB) basis include amendments and waivers to projects as well as some policy items that, as a result of discussion in Board committees and/or formal or informal meetings, are considered ready for approval without further discussion by the full Board. The 2005 Board Effectiveness paper clarified that any Executive Director may request Board discussion of an AOB item and that, if a Director wishes to be recorded as abstaining on or opposing an item without requesting Board discussion, the minutes which record the approval of the item will also record such abstention or opposition.\textsuperscript{67}

136. **Informal Meetings.** Informal Meetings are convened in order to provide a forum for exchange of views and for sharing information on matters of interest to the Executive Directors,

\textsuperscript{60} Toure Report, \textit{supra} note 11.
\textsuperscript{61} 1995 Review, \textit{supra} note 15.
\textsuperscript{62} Naim Report, \textit{supra} note 14.
\textsuperscript{63} 1988 Report, \textit{supra} note 13.
\textsuperscript{64} Article VI, Section 5(a).
\textsuperscript{65} Rules of Procedure for Meetings of the Executive Directors [Rules of Procedure], Section 2(f).
\textsuperscript{66} Id. Where the occasion is not a formal Board meeting, the Toure Report indicates that – in the President’s absence -- Committee of the Whole discussions are chaired by the responsible MD and informal meetings by an MD or VP. Technical Briefings may be conducted by an MD, VP, department director or senior staff. Toure Report, \textit{supra} note 11, at note 6, page 26. Note that the Executive Directors are not, strictly speaking, taking formal action as the Board on these latter occasions.
\textsuperscript{67} Board Effectiveness Paper, \textit{supra} note 10, paragraph 71.
often prior to the submission of a specific recommendation for Board approval. Decisions cannot be taken in informal meetings of the Executive Directors.

137. Formal and informal meetings are open to attendance by Executive Directors, their Alternates, the President and members of the staff designated by him, and such other persons as the Board may invite. Attendance is limited when the Board meets in executive session, to no more than three persons from each office, consisting of the Executive Director, Alternate Executive Director and one Temporary Alternate, and in restricted executive sessions, to one person per office.

138. Technical Briefings. Technical Briefings are convened in order to inform interested Executive Directors and their staff of work in progress on a particular subject. Attendance at Technical Briefings is considered optional and the legal provisions summarized above do not specifically apply to them. Whether particular policy papers are to be considered in Informal Meetings or Technical Briefings in advance of a formal discussion is arranged by Management in close consultation with the Executive Directors’ Steering Committee (discussed in paragraph 46 below). An Executive Director’s request for a Technical Briefing should be supported by at least five other Executive Directors. Technical Briefings scheduled at the request of Management should not exceed two per month.

139. Committee of the Whole. The Executive Directors may also meet as the Committee of the Whole, a committee made up of all Executive Directors. As is the case with Board committees generally, the role of the Committee of the Whole is limited to making recommendations or exchanging views on matters of interest to the Board. No decision binding on the Bank may be taken in these meetings. If required, the Board can take up the same issue for decision in a subsequent formal meeting. Traditionally, the Committee of the Whole has been used as a forum in which to hold preliminary discussions of issues before they were taken up by the Board. The Committee of the Whole is also the forum in which the Executive Directors act as a preparatory body for the work of the Development Committee.

140. Executive and Restricted Executive Sessions. These sessions are used when, in light of the sensitive and confidential nature of matters to be discussed, it is considered desirable to restrict attendance to Board meetings. Generally, these sessions are used for country confidential, market sensitive, personnel-related matters, and INT issues. Attendance to Executive Sessions is limited to three persons from each Executive Directors’ Office and at restricted executive sessions to one person per office.

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68 “Types of Board Meetings,” Memorandum to Executive Directors and Alternates from the Corporate Secretary, March 3, 1998. Prior to 1998, the Board also held Board Seminars, which were intended as informal gatherings used to explain a selected topic to the Executive Directors and to obtain their views, frequently in advance of a formal Board discussion.

69 Rules of Procedure, supra note 65, Section 2(d).

70 Toure Report, supra note 11, paragraph xxiv (iii).

71 Id.

72 Naim Report, supra note 14, paragraphs 16 and 53(a).

73 Board Effectiveness Paper, supra note 10, paragraph 77.
141. **Steering Committee.** The Executive Directors also meet in the Executive Directors’ Steering Committee, which is not a formally constituted committee of the Board. Its nature and functions are described in the Toure Report, as follows:

142. “[The Steering Committee is] an informal advisory body, whose functions include reviewing, with the assistance of the Secretary and Management, all matters relating to the scheduling and composition of the Executive Directors’ Work Program and other areas of interest related to the conduct of the Board’s business. Traditionally, the Steering Committee consists of the Dean, Co-Dean and the committee chairs. However, all Executive Directors are encouraged to attend Steering Committee meetings.”

4. **Board committees**

143. The Executive Directors are empowered under the Bank’s Articles to “appoint such committees as they deem advisable,” and committee membership is not limited to Executive Directors. Board Committees also cover IDA matters. Board committees have no decision-making power (except with regard to procedural or administrative matters) and committees do not vote on substantive issues. Instead, each committee submits reports and recommendations to the full Board. In case members of committees take different positions, the committee would report all views and indicate the degree of support received by each. The Board does not delegate decision-making power to the committees, because the weighted voting system under which Board decisions are taken only works if all Executive Directors participate in the decision.

144. Currently, there are five standing committees established by the Board: the Audit Committee, the Budget Committee, the Committee on Development Effectiveness (CODE), the Committee on Governance and Executive Directors’ Administrative Matters (COGAM), and the Personnel Committee. Rules of procedure for the standing committees have been established by the Board. These rules include that committee decisions on procedural and administrative matters are taken by simple majority of those present, and that committee reports to the Board indicate majority and minority views. Committee meetings are open to any Executive Director or authorized representative, “except in highly exceptional circumstances when the committee decides for stated reasons to go into closed session” and committee documents are circulated to all Executive Directors unless the committee directs otherwise. While these rules do not legally apply to the ad hoc committees and working groups that the Board establishes from time to time, the same principles are generally applied by reference.

145. The **Audit Committee** has a mandate to assist the Board in overseeing the World Bank Group’s financial condition, risk management and assessment processes, the adequacy of governance and controls, and reporting and accounting policies and procedures. This mandate includes, in particular, responsibilities relating to (i) the integrity of financial statements (IBRD, IDA, IFC, MIGA and trust funds), (ii) the External Auditor (appointment, qualifications, independence and performance), (iii) the Internal Audit Department, (iv) the system of internal controls regarding finance, accounting and ethics (including mechanisms for dealing with and

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74 Toure Report, supra note 11, paragraph 24.
75 Article V, Section 4(i).
76 Standing Committee Resolution, supra note 48, at paragraph 7.
minimizing fraud and corruption), (v) significant financial and reputational risks (for IBRD, IDA, IFC, MIGA and trust funds), and (vi) the effectiveness and integrity of financial policies in such areas as trust fund administration, procurement procedures and financial management, especially portfolio concentration, capital adequacy, the allocation of net income, and provisions for loss.

146. The **Budget Committee** considers certain aspects of Bank, IFC and MIGA business processes, administrative policies, standards and budget issues which have a significant impact on the cost effectiveness of their operations. The Committee regularly reviews the institutions' budgets for the coming fiscal year, as well as making midyear and retrospective reviews.

147. The mandate of **CODE** is to monitor and assess the Bank Groups' effectiveness in fulfilling its development mandate. The committee reviews the work of the Independent Evaluation Group for the World Bank Group, Management's Responses thereon, and select reports from Management to satisfy itself that the operations evaluation and self-evaluation activities are adequate and efficient. The committee also prepares for Board consideration select operations evaluations, draft strategies and policies, other high-priority development effectiveness issues, and monitors the implementation of Board decisions to ensure that the overall objective of poverty reduction is being served.

148. **COGAM** considers issues of governance and administrative policy relating to the Executive Directors and Alternates and their staff referred to it by the Board, or on the Committee’s own initiative, and makes recommendations to the Board. The Committee coordinates many of its recommendations with a similar committee established by the IMF Executive Board. In making its recommendations, the Committee tries to maintain a balance between the organizational and administrative objectives of the institution and the unique circumstances faced by the Executive Directors and Alternates in discharging their dual responsibilities.

149. The **Personnel Committee** is responsible for keeping under continuing review and, where appropriate, advising the Executive Directors on staff compensation and other significant personnel policy issues including strategic staffing, diversity and conflict resolution.

**C. Ethics**

150. A new Code of Conduct (COC) for Board Officials was adopted by the Executive Directors with effect as of November 1, 2007. It applies to Executive Directors and their Alternates, Senior Advisors and Advisors—collectively designated as “Board Officials”—, as well as the President of the Association. It sets forth principles and ethical standards for Board Officials in connection with, or having a bearing upon, their status and responsibilities in the organization, with a view to reinforcing ethical standards by “setting the tone at the top” and modernizing the ethics framework to reflect best practice. In general terms, the COC prescribes that Board Officials shall carry out their responsibilities as prescribed in the Articles of Agreement, the By-Laws, and other related documents, to the best of their ability and judgment. It stresses that Board Officials should maintain the highest standards of integrity in their personal and professional conduct and should observe principles of good governance. The Code also mandates that Board Officials shall hold the interests of the Bank Group paramount
over personal interests, and shall avoid conduct that could bring the Bank Group into disrepute or create the appearance of impropriety. It includes several specific provisions on conflict of interest, for which it adopts a more inclusive definition, and financial disclosure.

151. The Ethics Committee considers all matters relating to the interpretation or application of the COC, including requests for guidance concerning conflicts of interest, annual disclosures, or other ethical aspects of conduct in respect of Board Officials, and allegations of misconduct by Board Officials.

152. The Ethics Committee consists of five Executive Directors. They are appointed by the Executive Directors on the nomination of the Chairman of the Board following informal consultation with the Executive Directors, and in particular with the Dean. Membership of the Ethics Committee should reflect the economic, cultural, and geographic diversity of the Bank Group’s member countries. The Dean and Co-Dean are not eligible to serve as Committee Members. Specific procedures for the Ethics Committee are set out in the COC.
## Annex A: Attachment – Board Decision-Making

### 1. Institutional Issues

<table>
<thead>
<tr>
<th>Major Decisions</th>
<th>Sources</th>
</tr>
</thead>
<tbody>
<tr>
<td>IBRD President <em>ex officio</em> President of IDA</td>
<td>Article VI, Section 5(a)</td>
</tr>
<tr>
<td>Issue formal interpretations of Association’s Articles of Agreements and propose amendments</td>
<td>IDA Articles IX(a) and X(a)</td>
</tr>
<tr>
<td>Approve Association’s Annual Report</td>
<td>Article VI, Section II</td>
</tr>
</tbody>
</table>

1Sources are not comprehensive.

### 2. Operational Policy, Strategy and Instruments

<table>
<thead>
<tr>
<th>Major Discussions/Decisions</th>
<th>Sources</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Approve Policy Papers for the general operations of the Bank and grant any waivers thereto</td>
<td>Memorandum with Regard to Organization and Loan Procedure (Jun. 4, 1947); IDA Article VI, Section 2(h)</td>
</tr>
<tr>
<td>Discuss Country Assistance Strategies, Poverty Reduction Strategy Papers and Joint Staff Assessment Notes, and the related progress reports</td>
<td>Memorandum with Regard to Organization and Loan Procedure (June 4, 1947); Review of Board Procedures (R73-225; September 13, 1973); Mainstreaming of Guarantees as an Operational Tool of the World Bank (R94-145; July 14, 1994)</td>
</tr>
<tr>
<td>Approve specific financing operations (Credits, Guarantees and Grants), either through streamlined or regular procedures</td>
<td>Article VI, Section 2(b)(v)</td>
</tr>
<tr>
<td>Recommend cooperative arrangements with other international organizations for Governors approval</td>
<td>A Framework for Managing Global Programs and Partnerships (R2001-2; January 9, 2001)</td>
</tr>
<tr>
<td>Approve individual partnership arrangements requiring the involvement of the President</td>
<td>Article I</td>
</tr>
<tr>
<td>Approve Trust Funds providing assistance outside membership; or raising novel or significant issues; or when required in the respective instruments</td>
<td>Board Resolution No. IDA 93-10</td>
</tr>
</tbody>
</table>
### 3. Treasury, Finance, and Administration

<table>
<thead>
<tr>
<th>Major Discussions/Decisions</th>
<th>Sources</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discuss the Treasury Quarterly Reports</td>
<td></td>
</tr>
<tr>
<td>Review and Submit Bank’s financial statements to Governors</td>
<td>IDA By-Laws, Section 8</td>
</tr>
<tr>
<td>Set policy to ensure that Bank’s staff is of highest efficiency and technical competence and of wide geographical basis</td>
<td>Article VI, Section 5(d)</td>
</tr>
<tr>
<td>Approve annual budget</td>
<td>IDA By-Laws, Section 8</td>
</tr>
<tr>
<td>Call meetings of the Board of Governors and/or request Governors’ mail vote</td>
<td>IDA Article VI, Section 2(d) and (g)</td>
</tr>
<tr>
<td>Exercise general control over staff appointments, which are the responsibility of the President</td>
<td>IDA Article VI, Section 5 (b)</td>
</tr>
<tr>
<td>Receive advance notice of senior level appointments</td>
<td>Advance Notice of Senior Level Appointments (R73-146/1, July 3, 1973); Advance Notice on Managerial Appointments (R99-33, March 5, 1999)</td>
</tr>
<tr>
<td>Appoint Director General, Evaluation, members of the Inspection Panel and judges of the Administrative Tribunal (on nomination by President)</td>
<td>DGO Mandate, R2005-0226, October 27, 2005; Board Resolution No. IDA 93-10; Statute of Administrative Tribunal</td>
</tr>
<tr>
<td>Involved in selection process of Auditor General, Group General Counsel and Corporate Secretary (appointed by President)</td>
<td>2007 Legal Memorandum</td>
</tr>
</tbody>
</table>
THE WORLD BANK

IDA: INTERNAL CONTROLS REVIEW:

MANAGEMENT ASSESSMENT FY08

ANNEX B. SUPPLEMENTAL REPORT ON TRANSACTION-LEVEL CONTROLS
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IDART: INTERNAL CONTROLS REVIEW
MANAGEMENT'S SUPPLEMENTAL REPORT ON TRANSACTION-LEVEL CONTROLS IN IDA’S INTERNAL CONTROL FRAMEWORK

Executive Summary

1. As set out in paragraphs 12-33 of Management’s Scoping Memo for Part II\(^1\) (the “Scoping Memo”), in response to the recommendations of the Internal Auditing Department (IAD) and the Independent Evaluation Group (IEG) in their respective Part IB reports and discussion of Part IB work at the Audit Committee on July 16, 2007, during Part II Management has carried out the following supplemental work relating to transaction-level controls that included:

- assessments of the:
  - Analytic Advisory Activities (AAA) processes and controls, and compliance with these processes and controls;
  - Process for updating Operational Policy (OP) and Bank Procedures (BP)
  - Safeguards corporate risk management process;
  - IDA Credit/Grant Mix Determination;
  - IDA allocation process; and,
  - Quality Assurance Group’s (QAG) Quality of Supervision (QSA) 7 process;
- reviews of quality arrangements supporting financial management (FM) and procurement (PR) work in the context of IDA operations;
- identification of fraud and corruption controls at the transactions level; and,
- additional testing of Country Assistance Strategy (CAS) and Development Policy Loan (DPL) processes.

2. The results of this supplemental work have confirmed conclusions reached by Management under Part IB that the design and operational effectiveness of identified processes and associated key controls (including the additional processes and controls mapped and tested during Part II, listed below) are adequate to ensure compliance with IDA’s polices and procedures that funds are used for the purposes intended. In particular, during Part II, as part of compliance testing of transaction-level processes and controls, Management found 100% controls compliance in randomly selected transactions in: (i) the safeguards corporate risk management process, (ii) the process related to IDA Credit / Grant Mix Determination, (iii) IDA allocation process, (iv) Quality Assurance Group’s (QAG) Quality of Supervision (QSA) 7, and (v) additional CASs and DPLs.

3. The supplemental work also confirmed the significant deficiencies relating to:

- Timely accessibility of relevant documents;

\(^1\) See Annex C to the Report for details.
• Regional variances in financial management and procurement guidelines
• Not keeping pace with needed updates to OPs and BPs, particularly in the area of investment lending.

4. In addition, the Part II “drilldown” of fiduciary controls in the areas of PR and FM identified the following additional significant deficiencies:

• Adequacy of controls in place to ensure consistent follow-up on PR issues by the task teams, including the need for better integration of PR staff in task teams and clarification of accountabilities for procurement issues and decisions.
• Inconsistent implementation of PR post-reviews; and
• Inconsistency in quality arrangements for the documentation of FM supervision and some inconsistency in quality arrangements for oversight and monitoring of FM supervision.

5. Finally, the supplemental work also identified a significant deficiency in the AAA area in the need to simplify and rationalize processes and systems, taking into account the wide scope of AAA activities.

I. Introduction and Background

6. Background. As reflected in the IDA 14 Replenishment Report Management committed to carry out, during the period of IDA 14, an independent comprehensive assessment of its control framework including internal controls over IDA operations and compliance with its charter and policies, and making such assessment available to the public after its disclosure has been approved by IDA’s Executive Directors. The assessment has been conducted in the context of the internal control framework developed by COSO, adapted to fit the unique nature and operations of IDA. It has been carried out in three tiers: Management self-assessment; Independent Audit Department (IAD) review; and an independent evaluation of both by the Independent Evaluation Group (IEG). The assessment has

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2 See, Report from the Executive Directors of the International Development Association to the Board of Governors, Additions to IDA Resources: Fourteenth Replenishment, Working Together to Achieve the Millennium Development Goals, (approved by the Executive Directors of IDA on March 10, 2005), paragraph 39, under the Disclosure bullet.
3 COSO published a report in 1992, “Internal Controls – Integrated Framework,” which is widely referred to by leading financial institutions in the United States and is also seen as a model in many other parts of the world. IDA adopted the COSO framework as its controls methodology in 1995. The framework is an all encompassing process which covers all aspects of internal control of an organization’s operation. It considers not only the evaluation of formal controls, but also informal controls, such as ethics, trust, communication, organization behavior and leadership, and incorporates “top-down” as well as “bottom-up” analysis.
ANNEX B: SUPPLEMENTAL REPORT ON TRANSACTION-LEVEL CONTROLS

been divided into two parts: Part I, which focused on design and operating effectiveness of controls over IDA operations at the transaction level; and Part II, which focused on (i) entity-level controls, (ii) outstanding transaction-level controls deferred from Part I, and (iii) the operations objective of COSO.

7. **Objective and structure of this report.** This report reflects Management’s assessment of compliance at the transaction-level, building on work performed during Part I and supplemented by transaction-level work completed during Part II. In addition, Management’s work on transaction-level controls conducted during Parts I and II, as these relate to the third COSO objective, effectiveness and efficiency of IDA’s operations, are also reflected in the overall summary, IDA 14 Internal Controls Review.

8. Following this introduction, Section II of this report sets out the scope and methodology followed by Management in conducting supplementary work on transaction level controls during Part II. Section III sets out the results of Management’s assessment of transaction level controls, followed by a discussion of significant deficiencies identified by Management and recommended actions to address them. In accordance with document sharing process adopted under Part I, all documentation and testing results relating to the above were provided to IAD and IEG for their review and evaluation, respectively.

II. SCOPE and Methodology Summary

A. Scope

9. Throughout this assessment, Management followed the COSO definition of internal control, namely, a *process* affected by an entity’s board of directors, management and other personnel, designed to provide *reasonable assurance* regarding the achievement of objectives in three COSO categories: financial reporting, compliance and operations. Management assessed internal controls related to these three objectives categories against different expectations, an approach that was consistent with COSO. In the context of the compliance objective\(^4\), Management assessed whether IDA’s internal control system can be expected to provide *reasonable assurance* that IDA carries out its operations in compliance with its charter and operational policies. Following is a summary of the scope and methodology followed by management in assessing the compliance objective against such expectations:

10. The corporate entities for which the COSO framework was developed are subject to specific laws and regulations in their respective jurisdictions. IDA’s status as an international organization with immunities and privileges makes this COSO

\(^4\) The work done for the two other COSO objectives, financial reporting and efficiency and effectiveness of controls over operations, along with the assessment of entity-level controls, are covered in Annex A to the Report.
category not directly applicable. However, in addition to its charter (i.e. its Articles of Agreement) IDA has a body of internally generated policies and procedures with which it needs to comply. Management has therefore interpreted compliance with laws and regulations to mean compliance with IDA’s (i) Articles of Agreement, and (ii) operational policies and procedures.

11. Management’s assessment of IDA’s compliance with relevant provisions of its Articles of Agreement and operational policies and procedures was carried out in two parts. During Part I Management focused on transaction-level controls relating to compliance with (i) provisions of the IDA Articles of Agreement, as interpreted from time to time by IDA’s Executive Directors, relating to the management of IDA’s lending operations; and (ii) internal operational policies and procedures relating to the management of IDA’s lending operations. Management supplemented this work during Part II with additional work related to transaction-level controls associated with processes that were not covered during Part I, as well as a “drilldown” in the FM and PR areas.

12. In Management’s view, the overall results of its assessment show that the above methodology, made possible through the sequencing of assessment work undertaken and the methodology adopted by management, has yielded depth, specificity and relevance of findings and actionable recommendations.

13. In particular, to supplement Part I work, and in line with the Scoping Memo, the objectives of supplemental compliance testing work performed by Management during Part II were:

- **for FM and PR** to: (i) drill down on rationale for, and significance of, the regional variances in implementation of FM and PR guidelines identified in Part IB; and (ii) review the quality aspects that have been put in place in each region to support reviews and inputs of FM’s and PR relating to appraisal and supervision of projects;

- **for AAA** to: (i) map out the process of the main AAA product line, Economic and Sector Work (ESW) report; (ii) conduct a walkthrough; and (iii) test compliance of documents of ESW reports completed during FY2006-2007 that were randomly selected for this purpose, following the process similar to that performed for IL, DPL, and CAS product lines during Part I;

- **for OP/BP updates:** review and document the current processes underlying policy revision and update current status of OP/BP updates since completion of Part IB; and

- **for other modules:** complete the documentation, walkthroughs and testing for additional processes, namely: (i) safeguards corporate risk management process; (ii) IDA Credit/Grant Mix Determination; (iii) IDA allocation process; and (iv) QAG’s Quality of Supervision (QSA) process;

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5 In the area of FM, this included a review of issues relating to project audits, including audit TORs, audit review process and follow-up, as well as the relationship between the audits and SOE reviews.
• for anti-fraud and anti-corruption controls at the transaction level: identify links of transaction-level controls documented during Part I to entity-level anti-fraud and anti-corruption controls; and
• for CAS/DPL to expand the Part IB testing sample with additional transactions from regions not represented in these two processes.

14. Management’s findings relating to each of these objectives are set out in Section III of this Report.

B. Methodology

1. Financial Management and Procurement

15. Two separate review teams assembled by Management undertook a “drill-down” of FM and PR issues examining (a) the significance and appropriateness of variances in Regional implementation of FM and PR guidelines, and (b) the quality aspects supporting specialist inputs, defined for purposes of this review as Regional quality assurance (QA) arrangements. The separate reviews covered the following five areas:

• QA arrangements and business procedures;
• adequacy of resources;
• projects under preparation;
• projects during implementation; and
• documentation and communication.

16. The reviews did not evaluate the quality of FM and PR work. While these were closely related, a review of quality itself in these areas was beyond the scope of the reviews. Specifically, the “drilldowns” on FM and PR included: (i) a review of findings and recommendations of the QAG Quality of Supervision (QSA 7) assessment as it related to the areas of FM and PR; (ii) a review and incorporation, as appropriate, of IAD findings reflected in its recent fiduciary and project supervision audits; (iii) the development of separate questionnaires related to FM and PR that were filled out by the respective anchors and regional managers, (iv) a review of appropriate documentation from (and interviews with) anchor and regional FM and PR managers and specialists that supported responses to the questionnaires (these also helped the review teams determine whether follow-up of action plans described in Procurement reviews and FM assessments are done and identify current Quality review processes conducted on a portfolio-wide basis at the regional level); and (v) confirmation of procedures for the Management review of IL process from regional managers, particularly as they relate to risk assessment in the areas of FM and PR. The FM “drilldown” and resulting report was done in partnership with the FM anchor. The PR “drilldown” was similarly done in

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7 Management consulted with IAD during the development stage of the questionnaires and incorporated its comments in the final drafts of the questionnaires prior to distribution to respondents.
partnership with the PR anchor, however, the PR anchor took the lead in finalizing the PR report, given the uniqueness and complexity of the PR area. As per the document sharing process applied in Part I, all documentation and testing results were provided to IAD and IEG for their review.

2. Analytic and Advisory Activities

17. During Part II, Management (i) identified and mapped current processes and controls that apply to the main AAA product line, Economic and Sector Work (ESW), (ii) conducted a walkthrough of the mapped processes and controls, and (iii) tested compliance with such controls by a sample of randomly selected ESW reports completed and delivered to clients during FY07, in a process similar to that performed for IL, DPL, and CAS product lines during Part I. The focus on ESW (and for sampling purposes, on ESW reports) was in large part due to the fact that ESW funding has traditionally absorbed the major share of AAA funds and ESW reports account for over 80% of total ESW spending. In accordance with document sharing process adopted under Part I, all documentation and testing results relating to the above were provided to IAD and IEG for their review and evaluation, respectively.

3. OP/BP Updates

18. During Part I, Management identified that some OPs/BPs were not keeping pace with the changes needed and/or introduced on the ground, especially in the area of investment lending (IL). During Part II, Management therefore undertook to review and document the current processes underlying policy revision and make recommendations on how these processes could be made more efficient to facilitate more timely updates of operational policies and Bank procedures. In addition, in its Scoping Memo for Part II, Management noted that with the main fiduciary policies (including OP/BP 12.00 re disbursements and 10.02 re FM) issued in March 2007 and major instrument policies (including OP/BP 8.60 re DPLs and OP/BP 8.00, re emergency lending) in place, the issue of outdated OPs and BPs primarily affects the statements governing the appraisal and supervision of IL operations, i.e., OP/BP 10.00 and 13.05 and related statements. To this end, management has prepared a revised table of OP/BPs that have a direct bearing on IDA’s operations which shows the status of OP/BPs that were recently updated and flags those that still need to be updated/revised. Since most of these govern IL, during Part II, Management also assessed how the proposed reform and consolidation of IL policies will help address the issue of outdated OP/BPs.

19. The identification and documentation of processes underlying policy revision was led by OPCS in close consultation with LEG and assistance from the CSR mapping team. The process documentation was based on the experience with policy

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8 The sample was drawn from the universe of ESW Reports completed as of September 16, 2007, and whose cost exceeded $100,000. These types of ESW Reports accounted for 90% of ESW Reports completed. ESW as a whole has consumed approximately 67% of the AAA budget.
revisions of all types that took place over the past 4 years under OPCS leadership either as a sponsor for the needed policy revisions or as a coordinator of policy revisions sponsored/owned by other units. Examples of policy revisions sponsored by OPCS include: OP/BP 6.00, Expenditure Eligibility, OP/BP 13.20, Additional Financing, OP/BP 8.00, Rapid Response to Crises and Emergencies; examples of policy revisions sponsored by other units and coordinated by OPCS include: OP/BP 12.00, Disbursement, and OP/BP 14.40, Trust Funds). The processes underlying these policy reforms were identified and mapped using the same methodology as has been employed in mapping processes and key controls underlying transaction-level work performed during Part I. An “informal” walkthrough of these process flow charts was conducted with IEG and IAD. During this “walk-through” various questions were discussed and clarified. The final flow-charts that reflect the walkthrough were shared with IAD and IEG.

C. Other Modules:

1. Safeguards Corporate Risk Oversight

20. During Part II, Management (i) revised documentation for the Safeguards Risk Oversight (SRO) process Module # 29 to reflect the new guidance, 9 (ii) performed a walkthrough of the process when a project is flagged as having high corporate safeguard risk requiring enhanced oversight, and how a project is determined to no longer need enhanced oversight, and (iii) tested compliance of documents for projects currently subjected to the process and projects removed from the process during the most recent SRO review. The documents were randomly selected for this purpose. In accordance with document sharing process adopted under Part I, all documentation and testing results relating to the above were provided to IAD and IEG for their review and evaluation, respectively.

2. IDA 14 Grant Allocation Process: IDA Credit/Grant Mix Determination

21. Management also (i) identified and mapped the IDA Credit/Grant Mix Determination (Module #35) process, (ii) conducted a walkthrough of the mapped

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9 During Part I, the quality assurance and compliance unit responsible for review of safeguards (OPCQC) stated that the screening process for possible inclusion of projects onto the safeguards corporate risk list was based on close consultations between OPCQC and regional staff to determine potential risks and appropriate measures to address them, including potential inclusion on the corporate safeguards risk list. These consultations took place in different ways and on different cycles, depending on the project management system used in each region. Since this was originally designed as a management advisory system rather than as a specific control mechanism, the results of the screening and the subsequent decision to include or remove projects from the list were not recorded in a standardized manner. As a result, Management was unable to perform compliance testing on Module # 29 Safeguards – Corporate Risk List during Part IB. Management has taken steps to standardize the approach used by OPCQC and the regions in screening and tracking projects on the safeguards corporate risk list and provided guidance to the regions on this matter. This work was the subject of Management’s assessment in this area during Part II.
process, and (iii) tested compliance of documents of IDA-eligible countries in the FY07 IDA allocation that were randomly selected for this purpose. In accordance with document sharing process adopted under Part I, all documentation and testing results relating to the above were provided to IAD and IEG for their review and evaluation, respectively.

3. IDA 14 Grant Allocation Process: Debt Sustainability Analysis (DSA)

FY08 was the first year in which country eligibility for IDA grants has been mostly based on DSAs. With the understanding that these processes are still being fine-tuned, Management has mapped out the processes under the Debt Sustainability Framework, following the same methodology and framework used for testing Modules during Part I. Management has: (i) identified and mapped the Debt Sustainability Analysis (Module #34) process (ii) conducted a walkthrough of the mapped process, and (iii) tested compliance of documents of DSAs completed during FY08 that were randomly selected for this purpose. As per the document sharing process applied in Part I, all documentation and testing results were provided to IAD and IEG for their review.

4. QAG Quality of Supervision Assessment (QSA)

During Part I, Management documented and validated the Quality at Entry Assessment (QEA) process based on the recently completed QEAs. In the Scoping Memo, Management agreed with IAD and IEG that the QSA process would be tested for design and operating effectiveness during Part II. IAD conducted compliance testing on behalf of Management of documents completed for QSA that were randomly selected for the purpose. As per the document sharing process applied in Part I, all documentation and testing results were provided to IAD and IEG for their review.

10 During Part I, Management did not review the processes relating to the broader debt sustainability analyses required under IDA 14, including the grant allocation framework based on a country’s risk of debt distress. These new processes were in a very early stage of implementation during the testing period under review (July 1, 2005 – February, 28, 2006). More specifically, the forward-looking DSAs required for gauging a country’s risk of debt distress were not widely available. As agreed with the IDA Deputies, Management relied on a "static" method based on a country’s current debt situation as a temporary mechanism. In addition, confirmation from the IDA Deputies that eligibility for IDA grants would continue to be based on such new processes only took place in November 2006, as part of the IDA14 Mid-Term Review discussions – Debt Dynamics and Financing Terms: A Forward-Looking Approach To IDA Grant Eligibility.

11 FY08 samples were chosen, as the DSA process was formalized with the issuance of Staff Guidance Note on the Application of the Joint Bank-Fund Debt Sustainability Framework for Low-Income Countries (May 3, 2007).
5. **Tagging of Anti-Fraud and Corruption controls to all transaction level processes**

24. Following-up on an IAD recommendation, Management has reviewed the processes and transaction-level controls identified during Part I work and has linked, or “tagged”, each process or control to an entity-level anti-fraud and corruption control identified during Part II work. In accordance with document sharing process adopted under Part I, all documentation and testing results relating to the above were provided to IAD and IEG for their review and evaluation, respectively.

6. **Additional testing of CAS and DPL modules**

25. In its Part IB evaluation, IEG noted its concern over Management’s sampling methodology for the CAS and DPL modules that were tested for compliance with applicable policies and procedures. In order to address IEG’s concerns, Management undertook additional, targeted tests of these two modules during Part II, specifically including one CAS and one DPL from regions that did not have CAS and DPL transactions in the cohort of transactions that were randomly selected from the available pool of transactions during Part IB. Management tested compliance of documents from additional CAS and DPL samples from regions not represented in the initial testing.

### III. SUMMARY of Issues and Recommended Actions

#### A. Financial Management

26. The review found the following:

1. **Quality assurance arrangements and business procedures**

   - All Regions have QA arrangements that have been documented and disseminated to staff.
   - Regional QA arrangements have not been validated by the Financial Management Sector Board (FMSB).
   - It is difficult to ascertain in some Regions if QA arrangements for projects under implementation are completely in compliance with the Financial Management Practices Manual (FMPM).
   - There is a range of supplementary guidance for FM staff.
   - The information on some Region-specific websites is not current.

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12 During Part IB compliance testing, all relevant transactions from all regions were subject to the random selection process. The expanded testing of CAS and DPL controls during Part II ensured at least one representative transaction from regions in the combined Part IB and Part II CAS and DPL cohorts.
2. Adequacy of resources

- Regions report that they have the budgetary resources to fulfill their current fiduciary functions, and are able to plan and staff the FM function adequately.

3. Projects under preparation

- QA arrangements are operating effectively. Variances among Regions appear to be reasonable and generally responsive to the Region’s organizational structure and geographic and other constraints.

4. Projects during implementation

- Some Regions are not in full compliance with the QA arrangements that govern projects under implementation, and remediation is under way.
- Some gaps in the FM Network QA arrangements are not addressed in the Regional QA arrangements.
- Some QA aspects of management oversight during implementation are not operating effectively in some Regions.
- Many of the Regional variances in QA arrangements for projects under implementation make sense; however, in some Regions these variances represent risks and possible control gaps.

5. Documentation and communication

- While filing of FM documents has improved, there are issues surrounding the documentation of FM work.
- Besides using IRIS for filing and Region-specific websites for providing technical information, Regions maintain a number of different document repositories.
27. **Recommended action.** The FMSB already has actions under way to strengthen quality arrangements, including: (i) the CSR/OPCS Joint Evaluation of FM Network Quality Arrangements, which is beginning in FY09; (ii) implementation of PRIMA and full integration with other Bank systems and decision making processes, also in FY09; and (iii) review and update of the FMPM scheduled for completion during 2008. Management will incorporate findings from this review into the final methodology for the Joint Evaluation. Findings are also being taken into consideration in the update of the FMPM.

28. To address specific issues identified in the FM area, Management proposes the following actions:

- Regions will consolidate and update their QA arrangements (including QA-related information on their websites) by September 30, 2008. If necessary, these will be further updated and aligned with the FMPM, with support from OPCFM, immediately after the FMPM update is completed.
- Regions will update ARCS for all actions related to audits due in FY05 through FY07 by June 30, 2008. Regions with outstanding actions related to earlier years, will clear these backlogs by September 30, 2008. In addition, Regions will complete entry of baseline data on interim financial reports into PRIMA by October 31, 2008. The FMSB will monitor PRIMA and ARCS to ensure that the backlog is cleared and that, in future, data are entered regularly and promptly.
- Pending the establishment of the institutional Enterprise Content and Document Management system, the FMSB will develop and communicate good practices and additional guidance to staff by December 31, 2008.

B. **Procurement**

29. The review found the following:

- quality assurance arrangements for procurement are in place and are generally sound, and
- the regional variances identified are in line with the high degree of decentralization and broad mandate of the Regional Procurement Managers (RPMs).

However, management’s review also identified two issues that need to be addressed:

- adequacy of controls in place to ensure consistent follow-up on PR issues by the task teams, including the need for better integration of PR staff in task teams and clarification of accountabilities for procurement issues and decisions; and
- consistency in implementation of post-reviews.

30. In management’s view, these issues, combined with the findings of Part I of this exercise, rise to a level of a significant deficiency in PR area.

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13 This action has been completed, with the exception of Indonesia, and FM staff is working with the Region to resolve data entry issues specific to Indonesia.
31. Management proposes to address these issues through a set of monitorable actions as follows:

(a) Earlier and fuller integration of PR staff/tasks in all stages of project cycle, clarification of roles and accountabilities for PR matters within the task team:
   o Actions already completed:
     ♦ Starting in FY07, the procurement complaints database has been made a key control and management tool, and enhancements to the database include automatic alerts to remind RPMs of pending cases, to seek RPM clearance when closing cases, and to track complaints related to late payments. OPCPR monitoring of complaint follow-up has been strengthened.
     ♦ OPCPR has implemented an Anti-Money Laundering system and provides assistance on due diligence to the Regions who receive AML alerts thus preventing contract awards to firms on the UN/US/UK terrorist lists.
   o Actions planned:
     ♦ Full Integration of Procurement Staff and Tasks in Project Teams:
        OPCS will set up a working group by November 2008 to review the sharing of responsibilities between sector teams and procurement teams, for key procurement decisions at preparation and implementation stage, in particular reinstatement of requirement for RPM to clear PAD, TTL responsibility for document management and ISR ratings, and active monitoring of post review findings.
        OPCPR will support OPCS in the development of a Procurement Certification system specifically targeted for TTLs that would increase TTL awareness and importance given to procurement work, such system expected to be developed by December 2008 and rolled out during FY09.
     ♦ Strengthening OPCPR/PSB Roles
        PSB will review the potential benefits of strengthening and expanding the roles of the PSB and OPCPR to include identifying best regional practice and areas where it would be appropriate for regional variances of quality arrangements to be harmonized by December 2008.
     ♦ Fraud, Corruption and Governance
        In addition to developing a clear protocol between INT and the Procurement Network by October 2008, to dispose of complaints alleging Fraud and Corruption and handle cases where red flags have been identified, OPCPR will undertake a systematic review of any regional initiatives, including those in SARVP resulting from the India DIR of procurement in India’s health sector, on an ongoing basis (i) to address fraud and corruption and enhance governance and accountability during the project cycle, including
how to deal with red flags of corruption, and (ii) to develop measures as deemed appropriate.

- **Updating Procurement Policy and Procedural Framework and Policy Review**
  - OPCPR is updating OP/BP 11.00 Procurement by October 2008, to clarify responsibilities, update processes and procedures, and to reflect the enhanced complaint handling system. This exercise offers an opportunity to assess variances in regional practices and procedures falling below the threshold for the current policy exceptions mechanism, and to incorporate best practice into the policy and procedural framework.
  - OPCPR will review and update existing instructions (e.g. SWAp approaches) and identify new initiatives that need to be addressed (e.g. PPP, framework contracts, involvement of UN agencies, decentralized procurement).
  - OPCPR will update the existing template for the PAD Procurement Annex taking into account new initiatives, including risk-based procurement assessments with a focus on fraud and corruption by the end of 2008.
  - OPCPR will carry out a review of the preparation and use of Procurement Plans by the end of 2008.

- **Bank-wide Roll-out of Procurement Risk Assessment Tool**
  - The rollout of a dynamic Procurement Risk Assessment tool is expected to improve risk identification and monitoring in the PR area. This risk-based procurement assessment tool which was developed in SAR in 2004-05 and is in use in that Region has been further developed for Bank-wide use. The system is currently being mainstreamed by SAR/OPCPR and is expected to be available online in January 2009. It is mandated for use under the UCS proposal and expected to be mandated for Bank-wide use during FY09.

(b) Improving consistency of post-review implementation:

- Actions already completed:
  - A pilot automated post review system was launched in April 2008 to centralize the capture of all post review reports, including data, findings, and recommendations.

- Actions planned:
  - A post-review template to be used by all Regions is being developed by OPCPR and expected to be in place by the end of 2008. The template will ensure a harmonized approach to procurement post reviews and more consistent feedback into the ISR and Procurement Risk Assessment tool.
  - The date of the last post review and the status of implementing the mitigating actions will be recorded in the ISR beginning during FY09.
In parallel, a systems solution is being developed to track findings from PPRs and IPRs, expected to be put in place during FY09.

C. Analytic and Advisory Activities

32. Testing results showed an aggregate pass rate of 75%, measured as the total number of control steps in the sampled ESW reports found to be compliant. Most instances of non-compliances were random, isolated cases of failure to observe control requirements by those processing the ESW reports. It should be noted, however, that for roughly half of the non-compliance instances, controls were in fact observed, but because there were mismatches between dates recorded in SAP and the actual dates related to such controls (e.g. the dates of the Concept Review meetings of some of the transactions differed from the dates for such meetings recorded in SAP) Management recorded these as non-compliant.

33. **Recommended action.** Management is undertaking a broad review of the processes and controls, including systems and monitoring, that apply to AAA in order to simplify and strengthen them where needed, and ensure they are updated to take into account the wide variety of AAA currently carried out by the Bank. This review will also address the compliance weaknesses observed, along with other issues that have been raised by QAG in recent related reviews of AAA. Management expects to complete this review and discuss the recommended changes with the Board by late FY09.

D. OP/BP Updates

34. Management’s review and documentation of the current processes underlying policy revision have identified that the current processes appropriately differentiate between revisions that constitute policy changes that require approval of the Executive Directors as part of their policy setting and oversight responsibilities, and “housekeeping” changes in policy statements and procedures that fall within the responsibility of management.

35. While the process for initiating, preparing and endorsing policy changes that require approval of the Executive Directors are involved and time-consuming, management is of the view that the current process is appropriate for this level of change given the importance and impact of such changes on the control and operational framework of IDA. The process for introducing minor or “housekeeping” changes approved by management are much less involved and, at least in theory, can be done quickly and efficiently. As a result, management believes that the current backlog in OP/BP updates is not associated with the process for policy revisions as designed. Instead, the current backlog in policy updates stems from the prescriptive approach to policy and procedural statements (OPs and BPs) **drafting and content,** characteristic of the older policies. In such policy statements, policy “proper” could only be revised with the approval of the Board, and was often commingled with operating procedures and guidelines which require more frequent and timely management-approved changes. As a consequence, rather than making the minor changes as needed, such changes have tended to
accumulate and be absorbed in the much more involved and less frequent efforts of a major reform or change to the relevant policies. The principles-based approach reflected in the more recent policy reforms, which focuses the OP and BP statements on core principles and key controls, rather than detailed rules and procedures characteristic of the older statements, should help minimize any future backlogs in OP/BP updates.

36. **Recommended action.** During Part I, IL was identified as the most over-regulated Bank instrument and is subject to approximately 30 of the Bank’s operational policies and procedures, many of which are misaligned with the current practice and evolution of the IL instrument. This has contributed to the current lag on updating of OPs/BPs that apply to IL. To address this shortcoming, which has contributed to much inefficiency surrounding the current IL instrument, the IL reform effort will focus on consolidating and rationalizing the policies and procedures governing IL by creating a single principles-based “umbrella” policy for IL that would govern IL projects from preparation through completion. Reflecting lessons learned, including findings of this internal control review, the new IL policy would:

- reflect main principles governing IL;
- replace the current “one-size-fits-all” requirements with a risk-based approach to IL due diligence, processing, and design options; and
- replace the rigid “ring-fenced” project model with a flexible menu of design and funds flow options to better meet development and funding needs of IDA’s varied clients.

37. Management expects to make a proposal for policy consolidation during the second phase of IL reform, following the completion of (i) Phase I that would address preparation/appraisal process inefficiencies and significant deficiencies in supervision as a matter of priority, and (ii) broad consultations inside and outside the Bank to ensure that the new IL model meets and reflects the needs and expectations of the Bank’s clients, partners and shareholders. This second and final stage of IL reform is expected to be completed in FY10-Q2.

E. Other Modules

1. **Safeguards Corporate Risk Oversight**

38. On the basis of the (i) revised documentation, (ii) walkthroughs, and (iii) compliance testing, Management has confirmed that the safeguard corporate risk oversight process was functioning as designed.

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14 These include: OP/BP 6.00 related to expenditure eligibility, OP/BP 10.02 related to financial management, OP/BP 12.00 related to disbursement, OP/BP 13.20 related to additional financing and OP/BP 8.00 related to rapid response to crises and emergencies.
2. IDA 14 Grant Allocation Process: IDA Credit/Grant Mix Determination

39. No exceptions were found in the compliance testing and the process is deemed to be functioning as designed.

3. IDA 14 Grant Allocation Process: Debt Sustainability Analysis (DSA)

40. The compliance testing identified an exception in one of controls of one of the transactions tested which occurred prior to the release of guidelines on the processing of these transactions. Specifically, one of the transactions tested was missing an email showing approval of the relevant sector manager early during the process. This exception was not considered to be significant because this occurred prior to the release of relevant guidelines, and management found approvals by higher level managers in the succeeding stages of the process for this sample. Based on overall results of compliance testing for this module, management found the process to be functioning as designed.

4. QAG Quality of Supervision Assessment (QSA)

41. IAD found no exceptions to Management’s control attributes in the testing, and Management deemed the process to be functioning as designed.

5. Tagging of Anti-Fraud and Corruption controls to all transaction level processes

42. The results of this work have informed management’s entity-level assessment of fraud and corruption component. In accordance with document sharing process adopted under Part I, all documentation and testing results relating to the foregoing were provided to IAD and IEG for their review and evaluation, respectively.

6. Additional testing of CAS and DPL modules

43. On the basis of Part IB compliance testing, and compliance testing of additional CAS and DPL samples from regions not represented in the Part IB compliance testing, management has confirmed that both the CAS and DPL processes to be functioning as designed.
THE WORLD BANK

IDA 14 INTERNAL CONTROLS REVIEW:

MANAGEMENT ASSESSMENT FY08

ANNEX C.
ENTITY LEVEL CONTROLS AND EFFICIENCY AND EFFECTIVENESS OF INTERNAL CONTROLS SCOPING MEMORANDUM, FY08
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I. Background

1. Management is conducting a comprehensive assessment of internal controls over the International Development Association’s (IDA) operations and compliance with its charter and policies, which will be evaluated independently by IEG in response to the request of IDA Deputies reflected in the IDA 14 Replenishment Report.1

2. The assessment has been divided into two parts: Part I, which focused on design and operating effectiveness of controls over IDA operations at the transaction level; and Part II, which focuses on (i) entity-level controls, (ii) outstanding transaction-level controls deferred from Part I, and (iii) whether the internal control framework over IDA operations provides Senior Management and the Board reasonable assurance that they understand the extent to which IDA operations’ objectives are being achieved. The assessment is being carried out in three tiers (Management self-assessment, Internal Audit Department (IAD) review, and the Independent Evaluation Group (IEG) evaluation of both) in the context of the internal control framework developed by the Committee of Sponsoring Organizations of the Treadway Commission (COSO),2 adapted to fit the unique nature of IDA’s operational work. IEG expects to disclose its final report and other material after the Audit Committee (AC) and any Board discussions of the Part II report, following in this regard its usual practice.

3. To date, IEG has completed its evaluation of Part I of the assessment conducted by Management and the review carried out by IAD. As under Part I, during Part II, Management will closely consult with IAD and IEG on scope and methodology. As discussed with the AC, Management expects to complete Part II of its self-assessment by December 15, 2007.

II. SCOPE

A. COSO Control Framework

4. Consistent with the COSO definition of internal controls as a process that is designed to provide reasonable assurances3, Management will assess whether the

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1 See, Report from the Executive Directors of the International Development Association to the Board of Governors, Additions to IDA Resources: Fourteenth Replenishment, Working Together to Achieve the Millennium Development Goals, (approved by the Executive Directors of IDA on March 10, 2005), paragraph 39, under the Disclosure bullet.

2 COSO published a report in 1992, “Internal Controls – Integrated Framework,” which is widely referred to by leading financial institutions in the United States and is also seen as a model in many other parts of the world. IDA adopted the COSO framework as its controls methodology in 1995. The framework is an all encompassing process which covers all aspects of internal control of an organization’s operation. It considers not only the evaluation of formal controls, but also informal controls, such as ethics, trust, communication, organization behavior and leadership, and incorporates “top-down” as well as “bottom-up” analysis.

3 As it is currently published in its website: http://www.coso.org/publications/executive_summary_integrated_framework.htm
internal control framework is adequate to provide reasonable assurances to Senior Management and the Board in the three categories identified in the COSO framework, namely:

- **Reliability of financial reporting relating to IDA’s operations** – i.e. do the internal controls over IDA operations provide reasonable assurance to Senior Management and the Board that the published financial statements are being prepared reliably?
  - Since 1997, Management has annually asserted and received attestations from the external auditor that it maintains an adequate system of internal controls over external financial reporting for both IBRD (International Bank of Reconstruction and Development) and IDA.

- **Compliance with applicable laws and regulations in IDA’s operations** – i.e., do the internal controls over IDA operations provide reasonable assurance to Senior Management and the Board that “laws and regulations” governing IDA’s operations (i.e., (i) financial reporting regulations, (ii) IDA’s Articles of Agreement, and (iii) the Bank’s operational policies and procedures) are being complied with?
  - Financial reporting regulations, as required by the financial markets, are reviewed, documented, evaluated, and attested to by external auditors as part of the work performed for Management’s assertion of internal control over financial reporting;
  - Part I of the assessment focused on transaction-level controls relating to compliance with:
    - Provisions of the Articles, as interpreted from time to time by IDA’s Executive Directors, relating to the management of IDA’s lending operations; and
    - Internal operational policies and procedures relating to the management of IDA’s lending operations.
  - In addition, Part II will assess entity-level controls relevant to compliance with the Articles and operational policies and procedures and draw any relevant linkages between such controls and transaction-level controls relating to compliance that were assessed under Part I.

- **Effectiveness and efficiency of IDA’s operations** – i.e., do the internal controls over IDA operations provide reasonable assurance to Senior Management and the Board that they understand the extent to which IDA operations’ objectives are being achieved?
  - As discussed more fully in the next section, Part II of the assessment will examine whether the internal controls at the entity and transaction levels are effective in providing Senior Management and the Board reasonable assurance that they have the information from which they can understand the extent to which IDA operations’ objectives are achieved.

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III. ASSESSMENT Activities

A. Entity-Level Controls

5. As part of its initial Work Plan Management identified the control groups that form part of the internal controls framework over IDA’s operations and the specific control activities carried out by each such group. During Part II Management will map each such group to the COSO categories relating to “compliance” and “efficiency and effectiveness.” Such mapping will include the identification of (i) each group’s main responsibilities and role in the internal control framework over IDA operations; (ii) the primary products/outputs of each group relating to its role; and (iii) linkages between the roles and outputs of the groups in question. Such mapping will be corroborated by the information that would derive from the results of the entity level Questionnaire prepared by Management.

6. It is Management’s understanding that IAD, as part of its ongoing review activities, has initiated a preliminary review of the Bank’s entity-level controls. During Part II, Management will discuss the preliminary list of entity-level controls it identified with IAD to ensure consistency.

7. The entity level Questionnaire (see Attachment 1), developed based on source information available from the public accounting profession and the U.S. Government Accountability Office (GAO), has been adapted to meet the objectives of the IDA14 Internal Controls assessment. Questions relating to entity-level controls and antifraud programs and controls have been aligned with the five COSO components, namely (i) control environment, (ii) risk assessment or fraud risk assessment, (iii) control activities, (iv) monitoring, and (v) information and communication. It will be completed by all Bank units at the Senior Management level (Managing Directors, Vice-presidents, and Heads of stand-alone Departments -- the Quality Assurance Group (QAG), IAD, Department of Institutional Integrity (INT), Inspection Panel and IEG). Finance, Administration, and some Central VPUs and Departments (Treasury, CFP, ISG, CSR, HRS, GSD, IAD, INT, and EBC) have already completed the Questionnaire and follow-up process, per the schedule of the Bank’s annual Internal Control over Financial Reporting (ICFR) exercise. The Questionnaire was distributed to all other units in July.

8. The Questionnaire covers the following areas, as identified by individual COSO components:

• Control Environment: sets the tone of an organization and is the foundation for all other components of internal control.
  o Integrity, ethical values, and behavior of key executives
  o Management’s control consciousness and operating style
  o Management’s commitment to competence

5 See attachment 2 of the Work Plan discussed with the AC and the Committee on Development Effectiveness (CODE) on August 17, 2005 (AC2005-0092).
ANNEX C: ENTITY LEVEL CONTROLS AND EFFICIENCY AND EFFECTIVENESS OF INTERNAL CONTROLS SCOPING MEMORANDUM, FY08

- Organizational structure and assignment of authority and responsibility
- Human resource policies and practices

- Risk Assessment: the identification and analysis of relevant risks to the achievement of IDA operation objectives.
  - Entity-level objectives are established, communicated and monitored
  - Management has established mechanisms for identification of risks
  - Management evaluates and mitigates risks appropriately
  - Management has implemented mechanisms to anticipate, identify, and react to changes

- Control Activities: policies and procedures that help ensure the Management directives are carried out.
  - Operational practices followed and processes adequately documented
  - Management has clear objectives in terms of operating goals
  - Duties are adequately segregated
  - Policies are in place to control access to computer programs and data files

- Monitoring: a process that assesses the quality of the internal control system’s performance over time.
  - Management is responsive to internal and external recommendations
  - Internal audit’s scope, responsibilities, and audit plans are appropriate for the company
  - Internal audit adheres to professional standards, such as those issued by the institute of internal auditors
  - Internal communications are effective in providing feedback to Management on whether controls are operating effectively
  - There are regular self-assessment exercises in the Bank

- Information & Communication: identifying, capturing and communicating pertinent information in a form and timeframe that enables staff to carry out their responsibilities.
  - Operational reporting and related applications and information systems are reliable
  - Appropriate and necessary information is obtained from, and provided to, Management
  - Information is gathered from and disseminated to the appropriate people on a timely basis
o There is a process for identifying and responding to the changing information and communication needs

o Management communicates employees' duties and control responsibilities in an effective manner

o A "whistle-blowing" program has been established, and Management's reaction is monitored as it relates to operational matters

o Management's communication across and outside the company reflects an attitude toward sound internal controls

9. The Questionnaire is designed to solicit corroboration for answers provided by each respondent. The responses will be assessed as follows:

- Review of responses and supporting underlying documentation;
- Inquiries, either verbally through interviews or in writing or both, to drill-down where appropriate; and,
- Observations and analysis.

10. In addition to the mapping of entity-level controls and compilation, analysis and drill-down of the Questionnaire results, Management will also review the results of other corporate review activities – including, the Risk and Opportunity Workshop, the Letters of Representation exercise, and relevant IAD reports.

11. As part of this assessment, Management will also identify the primary functions of the Board, particularly as these relate to the COSO components of the “Control Environment” and “Information and Communication” (including “tone at the top,” ethics, culture) with respect to IDA’s overall internal control framework. Management notes that, during a meeting in April 2007, the Board requested its Committee on Governance and Executive Director’s Administrative Matters (COGAM) to make recommendations to the Board on issues of internal governance. In addition, Management has noted that a Sub-Group on Governance (SOG) was established by COGAM “to examine issues directly related to the recent leadership crisis, and broader issues of potential risk in other areas of the bank’s governance arrangements.” Management also understands that the SOG intends to present a document to the Board for its consideration by the Fall 2007 Development Committee meeting regarding some of the issues it will be reviewing. In light of this ongoing work, Management will not go beyond identification of the Board’s primary function. However, Management will review the issues to be reviewed by SOG prior to finalizing its Part II Report to determine their potential impact, if any, Management’s conclusions.

B. Issues Deferred to Part II

12. Analytic and Advisory Activities (AAA). During Part II, Management will (i) map out the process of the main AAA product line, Economic and Sector Work (ESW) reports, (ii) conduct a walkthrough, and (iii) test compliance of documents of ESW

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6 See Report to the Board from the COGAM greensheet of the meeting of July 11, 2007.
reports completed during FY2006-2007 that were randomly selected for this purpose, in a process similar to that performed for IL, DPL, and CAS product lines during Part I. The focus on ESW is based on the fact that ESW funding has traditionally absorbed the major share of AAA funds – for example, in FY2007, ESW accounted for 68% of the AAA budget of IDA and IDA-IBRD blend countries. Therefore, Management believes that the mapping and testing of the ESW process during Part II, Management will (i) help verify findings and recommendations of QAG relating to AAA activities overall and (ii) inform preparatory work underway in planning a larger-scale review of AAA in both IBRD and IDA. This work should also address some of the scope concerns expressed by IEG and IAD.

13. **Country Offices.** IEG has recommended that the assessment include country offices. Management agrees that country offices are an increasingly important part of IDA’s operational model. To this end, the application of internal controls over IDA operations at the country office level has been reflected in the work done to date at the transaction level and will be reflected in the entity level work for Part II. Specifically:

- During Part I, the document sample used to perform compliance testing of processes and key controls that apply to CAS, IL, and DPLs specifically included transactions (operations) that were task-managed from country offices and/or documents that were initiated, prepared and/or reviewed in country offices;
- During the ICFR, Management confirmed and the external auditor attested that: (i) all significant disbursement and procurement transactions include those from country offices, and are captured in the Bank’s systems and tested from headquarters; and (ii) all disbursement approvals are performed in headquarters, and all related controls have been tested in headquarters.
- The entity level Questionnaire distributed under Part II includes specific questions related to country offices in order to assess whether and how the application of the COSO components of IDA’s internal controls framework extends to these offices; and
- During Part II, Management will also review IAD’s FY2007 audits of country operations and take them into account in assessing the application/compliance with internal controls at the country-office level.

14. **Information Technology (IT).** As previously stated by Management, Part II will assess IT controls supporting IDA operations. In order to ensure that all IT controls related to key processes have been reviewed, Management has prepared an assessment matrix listing IDA operations business processes, the supporting underlying system applications, and the applicable underlying technology or software being used (see Attachment 2). These applications have been reviewed against the following objectives:

- Application systems implementation & maintenance
- Information systems security
- Information systems operations
- Systems software support
- Network support
- Database implementation & maintenance
15. As identified in the matrix, these objectives have been reviewed and associated controls have been tested during ICFR to assess whether such internal controls are adequate to ensure their operating effectiveness. Identified deficiencies have been described and evaluated as part of the ICFR assessment. There were no material weaknesses identified. However, during the ICFR review the following three IT-related issues were deemed to rise to the level of “Significant Deficiency”:

- Strengthening controls to prevent password policy breaches in SAP and other financial applications impacting financial reporting, by bank staff. This is in response to a finding by IAD, based on an audit of “Identify and Access Management” in FY07, which identified that SAP passwords are widely shared by Bank staff which may result in some unauthorized expenses in the financial statements;
- Strengthening controls around Information Security to rationalize and further limit privileged access to system applications and monitor changes made by IT staff using such privileged accounts; and
- Strengthening controls around Infrastructure Change Management to ensure that change management controls are applied consistently and exceptions are reviewed and authorized by appropriate authority.

16. During Part II, the actions implemented to mitigate these risks will be reviewed and assessed by Management.

17. In addition, during Part I Management found that many of the process controls that apply to IDA operations at the transaction-level (and particularly to the processes of CAS, IL and DPL) are not automated or otherwise entail consistent IT support. The linkage between this finding and the issue of document accessibility identified in Part I have led to the establishment of an expert panel to look into automation of work flow documentation and controls. Since this relates to future work, there is little that can be assessed during Part II. Management proposes to share with IAD and IEG the concept for developing automated workflow for IL and would welcome comments from IAD and IEG on this proposal. The one area where limited automated controls were introduced relates to the IT controls relating to supervision reporting through the Interim Status and Results Report (ISR). During Part II Management will coordinate with IAD to assess whether a review and assessment of these limited IT controls relating to the ISR will be necessary.

18. Finally, Management will continue to discuss with IAD any additional issues related to IT systems that may need to be reviewed and included during the Part II review.

19. Fraud and Corruption. An addition to the COSO framework that was specifically addressed within the final rules adopted by the Securities and Exchange Commission (SEC) under the US Sarbanes-Oxley Act was to ensure that the entity specifically reviews its fraud controls. Fraud is defined in SAS 99 as:
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“...an intentional act that results in a material misstatement in the financial statements that is the subject of an audit. Two types of misstatements are relevant to the auditor’s consideration of fraud – misstatements arising from fraudulent financial reporting, and misstatements arising from misappropriation of assets.”

20. Consistent with the above, the Bank’s fraud risk assessment is performed, in conjunction with the internal control evaluation for financial reporting, at the entity and significant account/process levels. These individual risk assessments are performed based upon Management’s overall knowledge of controls in place, new activities, products and ventures, and historical fraud.

21. In addition, following IAD’s recommendation, during Part II, Management will:
(i) assess controls over fraud and corruption at the entity-level, including controls to ensure that issues identified by fraud and corruption investigations are adequately addressed; and (ii) link, as appropriate, the entity-level fraud and corruption controls identified to the process or transaction-level controls designed to prevent or detect fraud and corruption. As a result of this work, Management will provide a listing of specific fraud and anti-corruption controls that have been identified at the transactional as well as entity levels. In performing its assessment, Management will also take into careful consideration the findings contained in the Volcker Panel Report relating to fraud and corruption controls specifically and the impact of these findings on the entity-level controls more generally.

C. Follow-up of Exceptions Cited in Part IB

22. Timely accessibility of relevant documents. As stated in paragraph 16 above, Management established an expert panel to look into automation of work flow documentation and controls. The panel was composed of representatives of all the regions, the Information Solutions Group (ISG), Controllers, Strategy and Resource Management (CSR) and Operations Policy and Country Services (OPCS). Draft recommendations concerning new workflow authorization and system-based new document retention requirements have been circulated to key parties in the operations community and will be vetted with Senior Management. These will be mapped into the new document retention system, and then piloted in one key process (investment lending (IL)). As stated in paragraph 16 above, Management proposes to share with IAD and IEG the concept for developing automated workflow for IL and would welcome comments from IAD and IEG on this proposal.

23. Follow-on work to assess: (i) the significance and appropriateness of variances in regional implementation of financial management (FM) and procurement guidelines, and (ii) quality aspects supporting specialist inputs. During Part II, Management will:

- Drill down on rationale for, and significance of, the regional variances in implementation of FM and procurement guidelines identified in Part IB; and
• Review the quality aspects that have been put in place in each region to support reviews and inputs of FM7, procurement, and safeguards specialists relating to appraisal and supervision of projects.

24. In performing this work, Management will (i) review findings and recommendations of the QAG Quality of Supervision (QSA-7) assessment as it relates to the areas of FM, procurement and safeguards; (ii) review and use as appropriate IAD findings reflected in its recent fiduciary and project supervision audits; (iii) collect appropriate documentation from and interview anchor and regional FM, procurement and safeguards managers and specialists to determine whether follow-up of action plans described in Procurement reviews and FM assessments are done and to identify current Quality review processes conducted on a portfolio-wide basis at the regional level; and (iv) review new procedures for Management review of IL, particularly as they relate to risk assessment in the areas of FM, procurement and safeguards.

25. Not keeping pace with the needed updates to OPs/BPs, particularly in the area of IL During Part I, Management identified that some OPs/BPs were not keeping pace with the changes needed and/or introduced on the ground. With the main fiduciary policies (including OP/BP 12.00 re disbursements and 10.02 re FM) issued in March 2007 and major instrument policies (including OP/BP 8.60 re DPLs and OP/BP 8.00, re emergency lending) in place, this issue primarily affects the umbrella OPs/BPs on appraisal and supervision of IL, i.e., OP/BP 10.00 and 13.05.

26. During Part II, Management will assess how the proposed reform and consolidation of IL policies will help address this issue. Management will also assess how the current processes for policy revisions could be made more efficient so as to facilitate more timely updates of operational policies and Bank procedures.

1. Status of all pending deficiencies/exceptions from Part I

27. During Part IA Management, IAD, and IEG identified specific issues with the documentation and design effectiveness of some key controls identified. These were combined and listed in a deficiency tracker that Management shared with IAD and IEG. At the end of Part I, Management reviewed all of these issues with IAD and IEG and resolved, where possible. During Part II Management will (i) drill down on transaction level control issues unresolved and entity level control issues deferred to Part II, and (ii) update IAD and IEG on the application of mitigating measures of issues where these had been identified. During Management’s review of Part II, open items/deficiencies identified by Management, IAD and IEG during Part I will be reviewed as to whether Management has resolved or remediated them as appropriate. Issues of efficiency and effectiveness will be tied into the specific areas being reviewed in Part II. As stated in its Part IB report, any unresolved issues/deficiencies that still remain unremediated at the end of Part II will be reviewed and evaluated by Management for their impact, individually and in aggregate, on IDA’s internal control framework over IDA operations.

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7 In the area of FM, this will include the review of issues relating to project audits, including audit TORs, audit review process and follow-up, as well as the relationship between the audits and SOE reviews.
2. Assessments of Modules to be Completed During Part II

28. **Safeguards Corporate Risk List.** During Management’s walkthrough processes the quality assurance and compliance unit responsible for review of safeguards (OPCQC) stated that the screening process for possible inclusion of projects onto the safeguards corporate risk list is based on close consultations between OPCQC and regional staff to determine potential risks and appropriate measures to address them, including potential inclusion on the corporate safeguards risk list. These consultations take place in different ways and on different cycles, depending on the project management system used in each region. Since this was originally designed as a management advisory system rather than as a specific control mechanism, the results of the screening and the subsequent decision to include or remove projects from the list were not recorded in a standardized manner. As a result, Management was unable to perform compliance testing on Module # 29 Safeguards – Corporate Risk List during Part IB.

29. Management has taken steps to standardize the approach used by OPCQC and the regions in screening and tracking projects on the safeguards corporate risk list and has provided guidance to the regions on this matter. During Part II, Management will revise documentation for module 29 to reflect the new guidance, perform a walkthrough of the process for being included on the list and being removed from the list. In addition, if sufficient data has been accumulated in order to test the application of the controls then an appropriate sample will be selected and tested by Management. As per the document sharing process applied in Part I, all documentation and testing results will be provided to IAD and IEG for their review.

30. **Debt Sustainability Analysis.** During Part I, Management did not review the processes relating to the broader debt sustainability analyses required under IDA 14, including the grant allocation framework based on countries' risk of debt distress. These new processes were in a very early stage of implementation during the testing period under review (July 1, 2005 – February, 28, 2006). More specifically, the forward-looking debt sustainability analyses (DSAs) required for gauging countries' risk of debt distress were not widely available. As agreed with the IDA Deputies, Management relied on a "static" method based on countries' current debt situation as a temporary mechanism. In addition, confirmation from the IDA Deputies that eligibility for IDA grants would continue to be based on such new processes only took place in November 2006, as part of the IDA14 Mid-Term Review discussions. As such, FY08 is the first year in which country eligibility for IDA grants has been mostly based on DSAs. With the understanding that these processes are still being fine-tuned, Management will map out the processes under the Debt Sustainability Framework. In addition, Management will review the paper being drafted for IDA Deputies on this topic to draw out any

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8 Management distinguishes: (i) the Debt Sustainability Framework (DSF) itself, which is a joint IMF-World Bank venture, and which provides guidelines and methodology for the debt sustainability analyses (DSAs); from, (ii) the IDA14 grants framework, which applies the DSF to establish countries' eligibility for grants. In the Bank, the DSF and the DSAs are under the purview of PREM’s Economic Policy and Debt Department (PRMED), while the IDA14 grants framework is under the purview of FRM.
preliminary conclusions and observations regarding the Debt Sustainability Analysis (DSA) tool that is part of the DSF.

31. **QAG Quality of Supervision Assessment.** During Part I, Management documented and validated the QEA process based on the recently completed QEA. It also agreed with IAD and IEG that during Part II, the QSA 7 process would be tested for design and operating effectiveness. In addition, as with all other work wherein IAD audits have been carried out, Management will take note of IAD’s findings and recommendations regarding QAG’s QSA process provided these are made available to Management before its Part II Report is finalized.

32. Management was informed that one part of the QAG assessment process was a quality assessment of fiduciary controls. As stated in paragraph 21, in order to substantiate any information gathered in the follow-up activities during Part II relating to fiduciary areas, the results in such areas of QSA 7 will also be reviewed, using an appropriate sample selected by Management. All documentation and testing results will be provided to IAD and IEG for their review. Action plans will be created for issues found, and will be tracked on the deficiency tracker, which will identify responsible units and staff and completion dates. In addition, as mentioned above, Management will take note of IAD’s findings and recommendations in these areas.

33. **Additional testing of CAS and DPL modules.** In its Part IB evaluation, IEG reported its concern over Management’s sampling methodology for the CAS and DPL modules that were tested for compliance with applicable policies and procedures. In order to address such concerns, Management agreed to conduct additional, targeted tests of these modules during Part II, specifically including one CAS and one DPL from regions whose CAS and DPL transactions were not tested (due to the limited pool of such transactions coming from such regions). As was done in Part I, Management will share its testing results with IAD and IEG.

**IV. PART II Report**

34. As was done during Part I, any deficiencies identified during Management’s assessment of Part II (including any that may remain unresolved from Part I after the follow-up work during Part II) will be placed on a summary deficiency tracker which will: (i) identify each deficiency, (ii) assess the deficiency type, (iii) assess mitigating controls over each deficiency, (iv) assess the potential financial impact of each deficiency as well as its impact from a non-financial perspective, and (v) set out Management’s proposed corrective action (remediation). Descriptions of any significant deficiencies or material weaknesses identified through its assessment will be set out in Management’s report, together with the respective remediation plans to address them. Management’s report will also summarize the findings and recommendations flowing from its assessment under Part II as well as its overall assessment. In particular, the report will set out Management’s views as to whether the internal control framework over IDA’s operations provides a reasonable assurance to Senior Management and the Board that:
ANNEX C: ENTITY LEVEL CONTROLS AND EFFICIENCY AND EFFECTIVENESS OF INTERNAL CONTROLS SCOPING MEMORANDUM, FY08

- the published financial statements are being prepared reliably,
- “laws and regulations” governing IDA’s operations (i.e., (i) financial reporting regulations, (ii) IDA’s Articles of Agreement, and (iii) the Bank’s operational policies and procedures) are being complied with, and
- they understand the extent to which IDA operations’ objectives are being achieved.

35. The report will be presented to the Steering Committee put together by Management for this exercise (which includes the heads of the following vice-presidential units: Operations Policy and Country Services, Controller’s Strategy and Resource Management, Concessional Finance and Global Partnerships, and Legal) for its endorsement prior to its submission to Senior Management, IAD, and IEG.

A. Timing of the Assessment

36. Management expects all responses on the Questionnaire to be turned in by mid-September 2007. Follow-up discussions are expected to be completed by mid-October 2007. A draft Management assessment will be shared with IAD and IEG in early December 2007. Management expects its assessment on Part II and the entire IDA internal control review will be completed by December 15, 2007. As Management proceeds with its assessment, it will keep IAD and IEG regularly informed on its work progress.

B. Internal Management Structure

37. The Part II assessment will continue to be led by the Offices of the Vice President CSR, and the Vice President, OPCS, with support roles for Concessional Finance and Global Partnerships (CFP) and Legal (LEG). The high-level Steering Committee comprised of the Vice Presidents of the four aforementioned VPUs with the inclusion of IAD and IEG Management as observers will continue to manage the implementation of this process, while the Project Management Team consisting of senior staff of these units will continue to implement the detailed work program.

C. Attestation Standard to be Used

38. As was described at the beginning of the IDA review, there are currently no existing prescribed guidelines or standards that organizations can follow that are specifically related to assessing and supporting the issuance of an assertion regarding the adequacy of internal controls over compliance with laws and regulations and operational efficiency and effectiveness. As such, Management will continue to use the same concepts as defined in the Auditing Standard No. 5 (AS5) issued by the PCAOB on May 24, 2007, An Audit of Internal Control That Is Integrated with An Audit of Financial Statements, together with recently issued guidance from the U.S. Securities and Exchange Commission (SEC) Regarding Management’s Report on Internal Control Over Financial Reporting as much as possible in performing its review.

39. Management believes that continuing to applying the concepts (as revised) that have been defined by standard setters for assessing internal controls over financial
reporting provides the level of comprehensiveness, rigor and standardization required in its self-assessment of internal controls.
Attachment 2
The IAD Review and Opinion
December 22, 2008

Mr. Jeffrey S. Gutman, Vice President & Head of Network, OPCVP
Mr. Fayezul H. Choudhury, Vice President & Controller, CSRVP

Report on a Review of
Management’s IDA 14 Internal Controls Review FY08 Assessment

Please find attached the final report for the above-mentioned review which was circulated earlier in draft form.

At this time, we would like to convey our sincere appreciation to management and staff for the courtesy extended to the audit team. If we can be of further assistance, please do not hesitate to contact us.

[Signature]

Carman L. Lapointe
Auditor General
Internal Auditing Department

Attachment

cc: Messrs./Mme. Zoellick (EXC); Daboub (MDD); Okenjo-Iweala (MDO);
    Wheeler (MDW); La Via (CFO); Le Houerou (CFPVP);
    Thomas (IEGDG); Gray (IEGWB)

KPMG
Review of Management’s IDA 14 Internal Controls Review FY08 Assessment

IAD Report No. IBRD FY09-18
December 19, 2008
Confidential

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IAD Review of Management's IDA 14 Internal Controls Review FY08 Assessment

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IAD Review of IDA 14 Internal Controls Review - Management Assessment

I. Background

As part of its FY09 work program, the Internal Auditing Department (IAD) has completed a review of "The World Bank IDA 14 Internal Controls Review – Management Assessment" (hereinafter referred to as Management’s Assessment) of IDA’s internal control framework including governance and entity-level controls. Management’s assessment was undertaken with a view to providing reasonable assurance to senior management and the Board that:

(i) IDA’s operations are in compliance with its charter and policies; and
(ii) IDA’s operations are carried out effectively and efficiently.

This assessment comprises the last of a three-part assessment in response to management’s commitment1 “to carry out an independent comprehensive assessment of IDA’s control framework including internal controls over IDA operations and compliance with its charter and policies”:

- Part IA assessed the design effectiveness of key controls currently in place to ensure compliance with the relevant Articles provisions and policies governing IDA’s operations;
- Part IB assessed the operating effectiveness of, or compliance with, the controls identified in Part IA; and,
- Part II assessed the efficiency and effectiveness of IDA’s operations, including governance and entity-level controls, as well as other outstanding items carried over from Part I.

II. Objective, Scope and Approach

In accordance with our Terms of Reference, IAD’s objective was to review the basis of management’s assessment, and express an opinion on whether it is fairly stated based on the criteria established in Internal Control – Integrated Framework issued by COSO.

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1 Management’s commitment was outlined in the IDA Fourteenth Replenishment report, approved by the Executive Directors of IDA in March 2005, which identified a monitorable action, targeted for CY05, the product of which was an ‘OED Assessment’.

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IAD’s review under Part II examined management’s assessment relating to the following:

- overarching control framework for IDA, including all aspects of corporate governance and entity-level controls;
- efficiency and effectiveness of IDA’s operations;
- information technology (IT) controls;
- fraud and corruption controls; and
- other outstanding items carried over from Part I, including (i) quality assurance arrangements for procurement and financial management in IDA’s operations (ii) three additional processes relating to Safeguards Corporate Risk, IDA’s Grant Allocation and Debt Sustainability, and Economic and Sector Work (iii) QAG’s Quality of Supervision Assessment, and (iv) additional testing of CAS and DPL modules.

IAD’s review of management’s Part II assessment was conducted during July 2007 – October 2008. As agreed with management, IAD applied relevant concepts of Auditing Standard 2 (AS2)², appropriately tailored for operational compliance controls.

IAD specifically performed the following:

- **Management Part II Scoping Memoranda:** IAD reviewed drafts of management’s Part II scoping memorandum received on July 24, 2007, August 9, September 16, September 18 and September 25, 2007. IAD provided specific comments on July 27 and August 21, 2007.

- **Management Questionnaires:** IAD reviewed management’s questionnaires for assessing entity-level controls and quality assurance arrangements for procurement and financial management, provided specific comments, and followed up on all comments.

- **Workshops/Review Sessions:** IAD attended process walkthrough sessions convened by management for three additional processes added in Part II (Safeguards Corporate Risk, IDA’s Grant Allocation and Debt Sustainability, and Economic and Sector Work) to validate process documentation, including flowcharts and narrative descriptions provided by management of key controls.

- **Revised Process Documentation:** IAD reviewed the revised process documentation reflecting required changes identified in workshops/review sessions.

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² Auditing Standard No. 2: An Audit of Internal Control over Financial Reporting Performed in Conjunction with Audit of Financial Statements (AS2) issued by the Public Company Accounting Oversight Board (PCAOB).
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- **Management Test Results**: IAD reviewed test results for Part II, provided by management between December 17, 2007 and August 4, 2008, including the documentary evidence supporting management’s conclusions.

- **Related IAD Audit Work**: IAD reviewed relevant results of independent internal audit projects to assess consistency with and reasonableness of management’s test results and conclusions, including the current status of remedial actions to address deficiencies identified in these audits. See Annex A for details.

- **Transmittals for Communicating Entity-Level Review Results**: IAD issued seven transmittals in March 2008 communicating preliminary review results related to management’s validation of business unit responses to the entity-level controls questionnaire.

- **Draft Management Assessment**: IAD reviewed the draft report and supporting annexes received on May 19 and June 3, 2008 and provided preliminary comments on June 18, 2008 with respect to the candor of management’s conclusions and consistency with the objectives and results of management’s assessment. IAD met with the IAD Controls Review Project Management Team, the Heads of the Procurement and Financial Management Sector Boards, and with staff from the respective anchors to discuss IAD’s comments. Management reformulated its overall conclusion to address some of IAD’s preliminary comments. IAD provided additional comments on July 29, 2008. IAD shared a preliminary version of its draft report on Aug 12, 2008 and subsequently met with management to discuss IAD’s comments. Management provided a revised version of its draft report and supporting annexes to IAD on October 8, 2008, taking into account several earlier IAD comments.

### III. Management’s Overall Conclusion

Management is of the view that the internal control system over IDA’s operations is adequate to provide reasonable assurance to senior management and the executive directors that:

- IDA’s published financial statements are being prepared reliably;
- IDA carries out its operations in compliance with the relevant provisions of its Articles of Agreement and operational policies and procedures; and,
- They are being made aware, in a timely manner, of the extent to which IDA is moving towards effective and efficient use of its resources in meeting its operational objectives.
ATTACHMENT 2: THE IAD REVIEW AND OPINION

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IV. IAD’s Opinion on Management’s Overall Conclusion

In our opinion, management’s assessment is fairly stated, taking into account the exceptions identified as significant deficiencies by management. However, in IAD’s opinion, the identified significant deficiencies relating to fiduciary controls, entity-level controls, IT controls, and fraud and corruption controls, in combination, could represent a material weakness, such that there is a reasonable possibility that internal control failures may not be prevented or detected in a timely manner to ensure IDA’s ability to meet its internal control objectives, unless remediated in a timely manner and effectively monitored on an ongoing basis.

V. General Observation

As noted in IAD’s Part IA and Part IB reports, this IDA assessment is the first comprehensive internal exercise undertaken by management to review its operational/compliance internal control framework. Furthermore, it appears to be unique in the multilateral development banking environment, and to our knowledge, in the broader international financial institution community. While the effort underlying the commitment was clearly underestimated at the outset, substantial commensurate benefits are anticipated: its results will provide a compelling baseline to identify opportunities for streamlining IDA’s (and concurrently IBRD’s) operations and internal controls while significantly improving consistency and efficiency.

VI. Specific Observations

1. Adequacy and Effectiveness of Key Fiduciary Controls

The results of compliance testing in Part IB indicated that approximately 21% of the key fiduciary controls did not operate effectively. Management’s Part II review of fiduciary controls has identified inconsistencies in regional quality arrangements for procurement and financial management, especially during project supervision, as well as the need to strengthen overall monitoring of quality.

While management has concluded that these deficiencies collectively constitute a significant deficiency in IDA’s system of internal control, it has nevertheless concluded that key controls are adequate to ensure compliance with IDA’s policies and procedures to ensure that funds are used for the purposes intended.

IAD concurs with management that the findings of Parts I and II on procurement and financial management collectively constitute a significant deficiency; however, in our opinion, management’s conclusion that the design and operating effectiveness of key

December 19, 2008

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controls are adequate to ensure use of funds for intended purposes, is not adequately supported and is inconsistent with results of management’s Part I & Part II assessments and with IAD’s independent audit results, for the following reasons:

- **Underlying Quality of Procurement and Financial Management Input:** Management’s assessment of procurement and financial management under Part II did not cover the quality of the underlying input. As indicated in IAD’s Part IB Report, an assessment of the underlying quality of procurement and financial management input is required in order to conclude on the operating effectiveness of these key fiduciary controls. Furthermore, independent IAD audits of country operations have shown that controls in financial management and procurement have not consistently operated effectively.

- ** Appropriateness of Regional Variances:** Gaps in oversight and/or quality assurance arrangements do not permit a determination of whether regional variances appropriately constitute compliance with policies, procedures and guidance. Management acknowledges that the appropriateness of regional variances should be assessed over time based on evaluations of the actual quality of fiduciary work.

- **Transaction Level Key Controls:** Part II testing indicated a need to redefine some transactional level key controls for procurement and financial management. Management is implementing comprehensive action plans to remediate deficiencies in these areas, many of which impact the design and/or operating effectiveness of controls identified as key controls in Part I.

As a result, in our opinion, any conclusion on the adequacy and effectiveness of key fiduciary controls to ensure use of funds for intended purposes would be premature until remediation plans have been implemented and verified as effective.

2. **Entity-Level Controls**

Management has concluded that there are significant deficiencies in IDA’s entity-level controls, specifically:

- issues relating to the current policy and procedural framework for investment lending;
- need for better integration of fraud and corruption issues into daily operations;
- inadequate mechanisms for risk aggregation and timeliness and consistency in monitoring, identifying and formulating an appropriate response to systemic risks;
- issues relating to AAA processes and controls; and,
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- controls over information systems relating to password sharing, privileged access, and infrastructure change management.

IAD concurs with management's assessment that there are significant deficiencies in IDA's entity-level controls. However, in our opinion, the following issues related to entity-level controls require further consideration:

**Governance Issues:** The COGAM Working Group Report on Internal Governance Outline July 3, 2008 identified governance issues that merit further attention and noted that the resolution of these issues would be critical for stronger internal governance and greater accountability. In our opinion, the identified opportunities for improvement relating to internal governance could also improve significantly the efficiency of IDA's operations.

**Issues from IAD Audits:** A number of independent IAD audits have highlighted the following issues relating to entity-level controls:

- **Governance and Accountability for Integrated Risk Management:** There is no institutional accountability for effective implementation of Integrated Risk Management. The most important steps in the adopted process, relating to risk response, remediation and enhancement, do not occur in the absence of systematic follow-up. The lack of effective implementation has serious implications for efficiency and accountability.

Management has initiated a comprehensive review to move towards an annual Integrated Risk Report by the end of FY09, that (i) describes the overall risks facing the organization (ii) inventories the various risk assessment activities (iii) identifies potential gaps and overlaps (iv) develops a dashboard of risk findings from various risk assessments, and (v) assesses the quality and consistency of the processes in place.

- **Oversight of Operational Risks:** Representations relating to business process management are neither adequately supported nor monitored at the institutional level. Consequently, issue resolution for business process and operational risks at the institutional level is weak. The primary issue relating to oversight over the process leading to the assignment of clear accountabilities for business process risk management at the Bank will likely require senior management review and decision.

To the extent that IAD's comments fall within the purview of Controller's, CSRVP has already initiated work to address the issues raised. Management plans to create a new integrated risk and control assessment tool that will combine elements of the existing Risk Scan and ROW tools and provide a more robust basis for VPUs to support representations on risk and controls.
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- **QAG Assessments:** Significant or pervasive deficiencies exist in QAG’s Quality-at-Entry Assessments and Quality of Supervision Assessments, affecting the achievement of QAG’s business objectives of providing staff and managers with credible, real-time feedback on quality. Transparency of the processes and lack of objectivity of input have contributed to reporting of success rates that are neither consistent with reality nor representative of the operations portfolio overall.

Senior Management has launched a review of QAG that will consider QAG’s role in relationship to other groups in the Bank and the overall institutional structure and arrangements for meeting key operational needs in tracking quality and providing essential and timely information to management. Based on the recommendations of this review, final decisions on next steps will be decided by senior management.

3. Efficiency and Effectiveness of Operations

Management concluded that the internal control system over IDA’s operations is adequate to provide reasonable assurance to senior management and the Board that they are being made aware in a timely manner of the extent to which IDA is moving toward effective and efficient use of resources in meeting its operational objectives.

However, as acknowledged by management, this conclusion with respect to efficiency and effectiveness of operations differed from the original objective reflected in the Part II scoping memorandum, namely, ‘do the internal controls over IDA operations provide reasonable assurance to senior management and the Board that IDA’s operations are carried out efficiently and effectively’. Management has noted that this revision was necessitated, given the many factors outside IDA’s control that may and often do affect the development impact and effectiveness of IDA’s operations.

IAD concurs with management’s conclusion relating to efficiency and effectiveness of operations. However, in our opinion, several opportunities exist for enhancing effectiveness and efficiency of IDA’s operations, including the following:

- **Reporting of Project Performance:** Quality and reliability of information in Implementation Status Reports on projects remain an issue. Management has acknowledged that lack of candor in reporting project risks diminishes the effectiveness of the current system of indicators in tracking portfolio performance, and reduces the likelihood that management will initiate timely corrective actions.

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3 For the purposes of this assessment, efficiency has been defined as “appropriate level of input to enable the business units to achieve the desired outcome;” effectiveness has been defined as “correct things are done and desired outcomes are being achieved.”

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Independent IAD reports have also concluded that significant deficiencies exist in the reliability of ratings on project performance. Management, as part of the first phase of Investment Lending Reform, intends to comprehensively address the issues relating to supervision reporting including more precise, candid, and timely reporting of risks and progress towards results.

- **IEG Outcome Ratings:** The percentage of projects with “satisfactory” outcome ratings for Africa, which is primarily IDA, as determined independently by IEG, has declined significantly⁴ from 72.2 in FY05 to 65.3 in FY06 and to 56.7 in FY07. In our opinion, given that *effectiveness* is defined for the purpose of this assessment as ‘correct things are done and desired outcomes are being achieved’, the significant control deficiencies in IDA operations identified in this assessment and in independent IAD reports are likely interfering with achievement of outcomes. Management has indicated that this issue has been extensively discussed with the Board, including the formulation of appropriate remedial actions.

- **Streamlining of Transactional Key Controls:** Opportunities identified during this assessment for streamlining of transactional key controls for procurement and financial management could result in significantly improved efficiency of IDA operations.

- **HR Practices:** Results of recent Bank-wide Risk Scans and the 2007 Staff Survey indicated concerns relating to staff skills and mix as well as resource deployment and performance management. HRSVP will develop a comprehensive roadmap/strategy for enhancing performance management and will continue its efforts to enhance the sharing and transparency of HR-related data.

4. **Information Technology Controls**

Management has stated that no material weaknesses were identified during the review of key IT systems during the FY07 Internal Controls over Financial Reporting (ICFR) review. However, certain processes surrounding password policy breaches, information security rationalization and monitoring of changes, and change management controls were identified by management as significant deficiencies requiring attention. In addition, several significant deficiencies in this area identified independently by IAD⁵ are currently being addressed, including issues relating to IT governance and strategy, business continuity management, information security management, and wireless security controls.

⁴ Refer to Bank’s Quarterly Business Review, Q1 of FY08.
⁵ Refer to IAD Report "IBRD FY08-33: Summary of Key Information Technology Issues reported by IAD during FY06-FY08".

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2-12
IAD Review of Management’s IDA 14
Internal Controls Review FY08 Assessment

IAD concurs with management’s assessment that issues relating to IT controls collectively constitute a significant deficiency.

5. Fraud and Corruption Controls

Management has identified specific key controls designed to prevent/detect fraud and corruption. However, significant deficiencies in these controls create vulnerabilities to fraud and corruption in countries where systemic corruption is not adequately addressed during program and project design.

In our opinion, these deficiencies are now being adequately addressed through the Bank-wide roll out of the procurement risk assessment tool, ongoing work on the Governance and Anti-Corruption (GAC) agenda, and management’s response to the India Detailed Implementation Review (DIR).

IAD concurs with management’s assessment that issues relating to fraud and corruption collectively constitute a significant deficiency.

VII. Status of IAD’s Part I Recommendations and Issues

Part IA

- Four IAD recommendations from Part IA are being currently actioned by management, (See Annex B); Eleven issues from IAD’s Part IA Deficiency Tracker remain open at the end of Part II and are being currently addressed by management. (See Annex C).

Part IB

- IAD’s observations relating to (i) auditing arrangements and (ii) the review of OP/BP 14.10 on debt reporting are being addressed by management; Six open issues from IAD’s Part IB transmittals are being actioned by management. (See Annex D).

Paekharrj Murugan
Auditor-in-Charge

Thomas Ho Quen Hum
Audit Manager
### Annex A
Related IAD Audit Reports Issued From FY07

<table>
<thead>
<tr>
<th>Report Number</th>
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<th>Report Date</th>
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<td>FY07-14</td>
<td>Audit of Bank Activities in Benin</td>
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<td>FY07-22</td>
<td>Audit of Bank Activities in Lesotho</td>
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<td>Audit of Bank Activities in Senegal</td>
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<td>Audit of AFR VPU</td>
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<td>Audit of Bank Activities in Pakistan</td>
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<td>Audit of the Process for Reporting Project Implementation Progress</td>
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<td>Audit of WBG Business Continuity Management</td>
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<td>Audit of Bank Activities in Ghana</td>
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<td>Audit of the Security and Controls over the Bank Wireless Network</td>
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<td>FY08-33</td>
<td>Summary of Key Information Technology Issues Reported by IAD during FY06-FY08</td>
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<td>Audit of the Quality Assurance Group</td>
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## Annex B

### Status of IAD Part I A Recommendations

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<tr>
<th>Issue</th>
<th>IAD Position at the end of Part II</th>
<th>Management Response/Action Plan</th>
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<tbody>
<tr>
<td>IDA Processes selected</td>
<td>Trust funds were excluded from the review; rationalization appears necessary to reconcile management’s interpreted scope with the original commitment.</td>
<td>Open: Management noted at the end of Part I that the approach followed proved to be preferable given the intensity, scope of work required and the real time limitations of what could be done in a resource constrained environment.</td>
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<tr>
<td>IT Controls</td>
<td>Certain automated controls in operations have not been examined.</td>
<td>Under implementation: These were not covered specifically as these areas were already identified as requiring further review and are being addressed currently by management.</td>
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<tr>
<td>Fraud and Corruption Controls</td>
<td>Management should explicitly identify and assess fraud and corruption related controls.</td>
<td>Under implementation: Management’s recommendations on actions needed to mainstream and integrate fraud and corruption issues into daily operations are set out in its response to the Volcker report.</td>
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<tr>
<td>Update of operational policies and procedures</td>
<td>Operational policies and procedures must be up to date with actual practices.</td>
<td>Under implementation: Updating and streamlining of policy framework governing investment lending is under way. Updates are also planned for operational policies and procedures relating to procurement and the FM Manual.</td>
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<tr>
<td>Document Retention and Accessibility</td>
<td>Timely accessibility of operational documents primarily relating to IL operations.</td>
<td>Under implementation: This is currently being implemented as part of the Enterprise Content Data Management (ECDM) effort.</td>
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<tr>
<th>Process</th>
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<th>Resolved: No Further Action Required (2)</th>
<th>Actioned and Closed During Part I (3)</th>
<th>To Be Actioned After Part II (4)</th>
<th>Deferred to Part II (5)</th>
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Annex C
Status of Items from IAD’s Part IA Deficiency Tracker
Annex D  
Status of IAD Part IB Transmittals

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<th>Process</th>
<th>Transmittals (1)</th>
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6 Management’s assessment did not include an analysis of compliance at the transaction level. Management had indicated that Part IB testing was not designed to assess compliance of a single given operation or product with all the applicable (key) controls throughout the project cycle.
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- Improving accountability for results.

IAD
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