

INTERNATIONAL DEVELOPMENT ASSOCIATION

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2009

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Throughout Management's Discussion and Analysis, terms in **boldface** type are defined in the Glossary of Terms on page 121.

The Management Discussion and Analysis contains forward looking statements which may be identified by such terms as "anticipates", "believes", "expects", "intends" or words of similar meaning. Such statements involve a number of assumptions and estimates that are based on current expectations, which are subject to risks and uncertainties beyond IDA's control. Consequently, actual future results could differ materially from those currently anticipated.

Section 1: OVERVIEW

International Development Association (IDA) is an international organization established in 1960 and is owned by its member countries. Since its inception IDA has played a pivotal role in the global aid architecture and is the largest multilateral channel for providing concessional financing to the world's poorest countries in their efforts to boost economic growth, lower poverty and improve the living conditions of people. Given its poverty focus, IDA directs a large share of its resources to countries where people earn less than two dollars a day.

IDA pursues these goals by providing concessional development credits, grants and guarantees to its borrowing member countries to help meet their development needs. It also participates in programs and initiatives including debt relief, and provides technical assistance and other advisory services to support poverty reduction.

Member contributions, internal resources (see **Section 5.3 Internal Resources**), and transfers from affiliated organizations, fund IDA's lending and grant making operations. As a result IDA does not borrow from the capital markets.

Commitment Authority and Cash Flows

IDA is a revolving concessional financing window with regular three-year **replenishments** by donors. The resources available to IDA for funding its grant financing, lending and guarantee activities constitute its **commitment authority**, which is measured in **Special Drawing Rights (SDRs)**. As commitments for development credits and grants are approved during the three year **replenishment** period, the **commitment authority** is drawn down. These committed funds are then disbursed over an extended period, averaging nine years.

The Fifteenth Replenishment of IDA (IDA15) is the current **replenishment** and runs from July 1, 2008 to June 30, 2011 with 45 donor governments contributing. The IDA15 **commitment authority** framework is SDR 27.8 billion, of which SDR 16.5 billion is funded by new donor contributions, SDR 4.1 billion from donors' compensation for Multilateral Debt Relief Initiative (MDRI), SDR 4.8 billion from internal resources including a carryover from previous **replenishments**, and the remaining SDR 2.4 billion from anticipated transfers from the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC). Of the total IDA15 **commitment authority** framework, SDR 8.4 billion was committed as of June 30, 2009.

IDA needs to have sufficient funds available to disburse approved development credits and grants.

Cash inflows consist of four primary components: (i) **encashment** of contributions provided by donor countries; (ii) transfers from IBRD's net income and grants from IFC's retained earnings; (iii) credit reflows, including principal repayments and income from development credits and guarantees; and (iv) investment income on liquid assets. Cash outflows have two primary components: (i) disbursements of approved credits and grants; and (ii) payments to IBRD for IDA's allocated share of the combined administrative expenses.

IDA faces timing mismatches between cash receipts from donors and borrowers and disbursements of new credits and grants. To manage these timing mismatches between cash inflows and outflows and to ensure optimal use of development resources, IDA employs a number of financial practices, namely:

- Donor funds are encashed over time so as to match the nine-year average disbursement profile of development credits and grants.
- Provision of incentives to donors for early **encashments**.
- Expected principal repayments on disbursed and outstanding credits are considered as a source of **commitment authority**.
- Projected future investment income is committed at the beginning of each **replenishment** period.
- Total income from credits and guarantees is expected to cover administrative expenses in a given year.
- Use of various **hedging** strategies to minimize currency mismatches of cashflows.

Basis of Reporting

IDA's financial statements are prepared in conformity with the accounting principles generally accepted in the United States of America (U.S. GAAP).

Members' subscriptions and contributions are recorded on the balance sheet since they confer an equity participation in the net assets of IDA through **voting rights**. Subscriptions and contributions can be used to fund development grants and the costs of providing debt relief under Heavily Indebted Poor Countries (HIPC) Debt Initiative and MDRI. Under U.S. GAAP, development grants and adjustments to the accumulated provision for debt relief and losses on development credits and guarantees are recorded as a charge against or addition to income.

This accounting under U.S. GAAP creates an asymmetry in IDA's Statement of Income to the extent that subscriptions and contributions fund

development grants and are used to bear the costs of debt relief. This asymmetry has resulted in IDA recording losses in its income statement over the years. These losses have had no impact on the financial and operational management of IDA at any point in time. IDA's financial and operational management is driven by:

- its lending capacity as determined by the **commitment authority** of the particular **replenishment** effective at that time (see **Section 5 Financial Resources**); and
- having sufficient liquidity available on a timely basis in the amount needed to meet future cash flow requirements, including disbursements for credits, grants, and administrative expenses (see **Section 7 Management of Liquid Asset Holdings**).

IDA uses currency forward contracts to hedge its exposure to any potential loss of value of contributions in national currencies vis-à-vis the **SDR** pledged by donors at the start of the **replenishment**. The translation adjustment on the non-functional currencies of these forward contracts is reported in the income statement. However the economic offset, the change in value of donor pledges, is not reported in IDA's financial statements, since donor pledges do not meet the definition of assets.

Section 2: FINANCIAL RESULTS

2.1 Current Economic Conditions

IDA has had only limited exposure to the current market conditions since its liquidity portfolio had minimal exposure to asset classes which suffered

during the economic crises and it does not borrow from the capital markets. As a result, IDA's lending capacity, as determined by its **commitment authority** Framework, has not been affected.

2.2 Net Income (Loss)

Table 1 Condensed Statement of Income provides a comparison of the main sources of income and expenses for the two years under review.

FY2009 net income reflects an increase of \$2,133 million over that of FY2008. The factors contributing to this increase are discussed below.

Income from development credits and guarantees in FY2009 declined by \$120 million in comparison with FY2008. This was primarily due to credits outstanding to three member countries being restored to accrual status in FY2008, and the resultant recognition of income accreted in prior years' being recognized in FY2008. In addition, commitment charges were reduced from 10 basis points in FY2008 to nil in FY2009.

IDA's investment portfolio has a **duration** which is determined based on its liquidity management strategy. The majority of the portfolio (Tranche 1) is invested to immunize contracted future net cashflow requirements, which generally extend up to nine years at the start of a **replenishment**. The length of this **duration** position makes IDA's investment portfolio's mark-to-market value sensitive to interest rate movements. IDA's investment gains/losses are economically offset by increases/decreases in the present value of IDA's future net cashflow requirements.

Table 1 Condensed Statement of Income

Expressed in millions of U.S. dollars

	FY 2009	FY 2008
Income		
Income from development credits and guarantees	\$801	\$921
Net investment income	1,499	1,006
Transfers and grants from affiliated organizations and trust	1,037	1,104
Expenses		
Administrative expenses	(975)	(888)
Development grants	(2,575)	(3,151)
Release of provision for debt relief and for losses on credits and guarantees	1,236	773
Other expenses, net	(45)	-
Items relating to hedging of donor contributions		
Non-functional currency translation adjustment gains	859	6
Net unrealized losses on non-trading derivatives	13	(54)
Net Income (loss)	\$1,850	\$(283)

During FY2009, there were significant downward shifts in U.S. dollar, euro and British pound sterling interest rates compared to FY2008, resulting in significant mark-to-market gains which contributed to the increase in investment income of \$493 million over the previous year.

During FY2009, IDA received \$583 million as transfers from IBRD and \$450 million as grants from IFC. The grants from IFC are to be used as part of IDA15 resources in furtherance of IFC's purposes. During FY2008, IDA received \$600 million from IBRD and \$500 million as grants from IFC. An additional amount of \$4 million was received from trust funds in both years.

Administrative expenses increased by \$87 million over the prior year primarily due to increases in staff costs including pension benefit costs.

The \$576 million decrease in grant expenses over the prior year was mainly due to the pre-arrears clearance grants to Liberia and Côte d'Ivoire in FY2008.

FY2009 saw an increase in the release of provision for debt relief and for losses on credits and guarantees of \$463 million compared to FY2008.

The main driver of this increase was Nepal's decision in February 2009 not to seek eligibility under the HIPC Debt Relief Initiative.

The increase in non-functional currency translation gains of \$853 million reported during FY2009 was due to the impact of depreciation of national currencies of donors against the U.S. dollar on derivative liabilities relating to hedges of donor commitments. These hedges were entered into in May 2008.

2.3 Financing Operations

A summary of the financing operations for the last three fiscal years is included in **Table 2**.

Commitments of development credits and grants in FY2009 increased by \$2,806 (25%) million over those in FY2008. In terms of regional focus, Africa and South Asia together account for 86% of the FY2009 commitments (see **Chart 1**).

Net disbursements increased by \$32 million over the same period. In FY2008 **net disbursements** were higher than normal due to pre-arrears clearance grants to Liberia and Côte d'Ivoire in FY2008.

Table 2: Financing Summary and Selected Financial Data

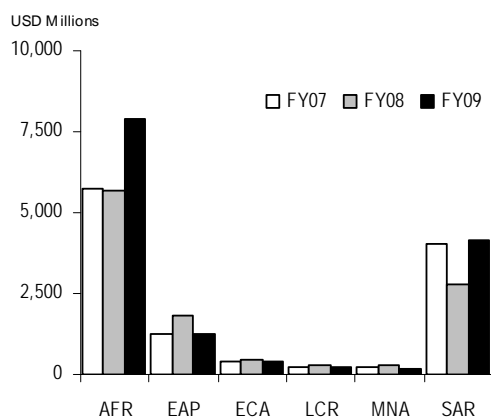
In millions of U.S. dollars

As of or for the fiscal years ended June 30

	2009	2008	2007
Financing			
Commitments of credits, grants and guarantees	\$14,041 ^a	\$11,235	\$11,867
Gross Disbursements	9,219	9,160	8,579
of which development grants	2,209	2,626	1,289
Net Disbursements including grants	7,010	6,978	6,826
Key Balance Sheet Data			
Total Assets	\$146,010	\$149,849	\$131,839
Development Credits outstanding	112,894	113,542	102,457
Net Investment Portfolio	21,287	19,053	17,469
Subscriptions and Contributions paid-in	150,085	142,416	136,091

a. FY2009 commitments of credits and grants include HIPC grants totaling \$46 million.

Chart 1: Commitments of Credits and Grants by Regions



Section 3: DEVELOPMENT ACTIVITIES

3.1 Eligibility criteria

Two basic criteria govern a country's eligibility for IDA resources: relative poverty defined as gross national income (GNI) per capita below an established threshold (updated annually), and lack of creditworthiness to borrow on market terms and therefore, a need for concessional resources. Currently, seventy-nine countries are eligible to borrow from IDA. Of these, sixty-five are not considered sufficiently creditworthy to borrow from

the International Bank for Reconstruction and Development (IBRD) and are referred to as "IDA only" countries. The remaining fourteen are deemed to have limited IBRD creditworthiness. These latter countries may receive both IDA and IBRD financing and are referred to as "blend" countries. With a few exceptions, IDA's eligibility cutoff for FY2009 was a per capita Gross National Income (GNI) in 2007 of \$1,095 (the "operational cutoff"). The FY2010 operational cutoff has been set at \$1,135.

3.2 Financing Principles

IDA's financing operations are required to conform to the general principles derived from its Articles. These principles (which are described in **Box 1**), taken together, seek to ensure that IDA financing is made to member countries for financially and economically sound purposes to which those countries have assigned high development priority, and that the financing is utilized as intended. Within the scope permitted by the Articles, application of these principles must be developed and adjusted in light of experience and changing conditions.

Box 1: Financing Principles

- (i) IDA may provide financing in the form of development credits, grants and guarantees directly to its members, public or private entities and regional or public international organizations.
- (ii) IDA's financing is designed to promote economic development, increase productivity and thus raise standards of living in its member countries. Investment projects financed by IDA are required to meet IDA's standards for technical, economic, financial, institutional and environmental soundness. Specific provisions apply to development policy financing, including the treatment of the macroeconomic framework, poverty and social impact, environment, forests and other natural resources.
- (iii) Decisions to approve financing are based upon, among other things, studies by IDA of a member country's economic structure, including assessments of its resources and ability to generate sufficient foreign exchange to meet debt-service obligations.
- (iv) IDA must be satisfied that in the prevailing market conditions (taking into account the member's overall external financing requirements), the borrower would be unable to obtain financing under conditions which, in the opinion of IDA, are reasonable for the borrower. This would include loans made by private sources or IBRD.
- (v) The use of financing proceeds is supervised. IDA makes arrangements intended to ensure that funds provided are used only for authorized purposes and, where relevant, with due attention to considerations of cost-effectiveness. This policy is enforced primarily by requiring borrowers (a) to submit documentation establishing, to IDA's satisfaction, that the expenditures financed with the proceeds of development credits or grants are made in conformity with the applicable financing agreements, and (b) to maximize competition in the procurement of goods and services by using, wherever possible, international competitive bidding procedures or, when it is not appropriate, other procedures that ensure maximum economy and efficiency. In addition, under pilot programs approved by the Executive Directors, IDA considers the use of borrower country procurement, and environmental and social safeguard systems in selected operations where these systems are assessed by IDA as being equivalent to IDA's systems and where the borrower's policies and procedures, implementation practices, track record, fiduciary and safeguard risks and capacity are considered acceptable to IDA.

3.3 Financing Cycles

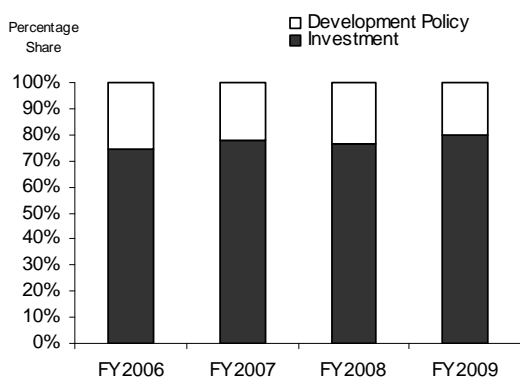
The process of identifying and appraising a project and approving and disbursing the funds often extends over several years. After appraisal of a project by staff, with certain exceptions, IDA's Executive Directors must approve each credit or grant.

Disbursements are subject to the fulfillment of conditions set out in the credit or grant agreement. During implementation of IDA supported operations, staff review progress, monitor compliance with IDA policies, and assist in resolving any problems that may arise. An independent unit, the Independent Evaluations Group, assesses the extent to which operations have met their major objectives, and these evaluations are reported directly to the Executive Directors. However, on numerous occasions, IDA has shortened the preparation and approval cycle in response to emergency situations, such as natural disasters and financial crises. The establishment of *IDA Financial Crisis Response Fast-Track Facility* (see **Section 4.6 Financial Crisis Response Fast Track Facility**) is an example.

3.4 Financing Categories

IDA's financing falls into one of two categories – investment lending or development policy lending. Investment lending is generally used to finance goods, works, and services in support of economic and social development projects in a broad range of sectors. In contrast, development policy lending provides quick disbursing credits or grants to members with external financing needs to support structural reforms in a sector or the economy as a whole. They support the policy and institutional changes needed to create an environment conducive to sustained and equitable growth. The share of investment lending has remained fairly consistent at between 74% in FY2006 and 80% in FY2009 as illustrated in **Chart 2**.

Chart 2: Share of Lending Categories



3.5 IDA's Policies for Poverty Reduction

The Poverty Reduction Strategy (PRS) approach followed by IDA is an important step in the

evolution of the country-based development model which recognizes recipient country governments as the most important stakeholder, brings a clearer focus on poverty reduction, emphasizes national ownership of the development effort, and creates accountability for development results. Alignment with the PRS is the cornerstone of IDA's support to the country-based development model and the Country Assistance Strategy (CAS) provides an anchor for IDA's support at the country level.

The CAS facilitates alignment with country priorities by taking into account national development programs as well as harmonization with other donors and World Bank Group activities, thereby maximizing impact. The CAS also makes it possible for IDA's program to reconcile global concerns and national priorities at the country level. Finally, IDA provides support for the strengthening of national capacities, including those for environmental and social safeguards, as well as public financial management and procurement.

Section 4: PRODUCTS AND PROGRAMS

The financial terms of IDA's products are described in detail below.

4.1 Development Credits

Currencies

Currently all development credits approved are denominated in **SDRs**. Before August 1, 1980, IDA credits were denominated in U.S. dollars. Principal payments and service and commitment charges are due in the currency specified in the Development Credit Agreement in an amount equivalent to the **SDRs** required under the agreement.

Charges on development credits

IDA's policy is to maintain its charges (service and commitment charges) at a level that will cover its projected administrative expenses.

Service Charges. A service charge is levied on the principal amount disbursed and outstanding on all development credits, regardless of eligibility by repayment terms, at the rate of 0.75 percent per annum, to cover the administrative expenses of IDA.

Interest. Interest is charged only on hard-term credits. The interest charged is more concessional than the prevailing IBRD lending rate and is set at 200 basis points below the equivalent IBRD lending rate in fixed-rate terms. The actual rate is determined on an annual basis, prior to the start of each fiscal year and applies for all hard-term IDA credits approved during a fiscal year. For FY2009 the interest rate was 3.2 percent. For FY2010 the interest rate is set at 3.52 percent.

Commitment Charge. A commitment charge is payable on the undisbursed amount of the development credit. The Executive Directors set the commitment charge at the beginning of each fiscal year. Commitment charges are set having regard to the extent that service charges, adjusted to include income forgone from development credits forgiven under HIPC and MDRI, and income forgone as a result of providing grant financing (instead of development credits), cover administrative expenses. For FY2010, IDA's Executive Directors have retained the commitment charge at zero. **Table 3** shows the history of IDA commitment charges on undisbursed development credits.

Table 3: Commitment Charges on Credits

<i>Fiscal Year</i>	<i>Commitment charge on undisbursed development credits in basis points</i>
FY 2003 and prior	0
FY 2004	50
FY 2005	35
FY 2006	30
FY 2007	20
FY 2008	10
FY 2009	0
FY 2010	0

Repayment Terms

Development credits approved through June 30, 1987 have a final maturity of 50 years including a grace period of 10 years. IDA credits approved after that date also have a grace period of 10 years but the final maturity and repayment schedule depend on whether the borrower is classified as **IDA-only** or **blend**. **Table 4** provides a summary of the repayment terms of development credits based on eligibility.

4.2 Development Grants

Commitment Authority for and funding of Grants.

Only funds that are provided with specific grant authorization may be used to finance IDA grants.¹ Beginning with the transfer out of IBRD's FY1997 net income, funds received from IBRD as net income transfers have included explicit authority that the funding could be used for grants. Recent **replenishment** resolutions have authorized the financing of grants from donor resources. In addition, all grants received from IFC's retained earnings have also included the explicit authorization that IDA could use such funding for grants.

¹ IDA's Articles of Agreement (Article V, Section 2(a)) state, "financing by the Association shall take the form of loans." IDA may provide financing in different form, such as grants and guarantees, only if the funds for such financing are accompanied by express advance authorization for such other form of financing. The restriction also applies to "funds derived therefrom as principal, interest or other charges," i.e. reflows.

Commitment charges on the undisbursed balances of grants are set annually by the Executive Directors of IDA. From FY2003 through FY2010, IDA's commitment charge on the undisbursed balances of grants has been set at zero.

Allocation of Grants

Grants in IDA15 are available solely for IDA-only countries. The amount available for each country is a function of the country's performance-based IDA allocation (see **Section 6 Allocations of Resources**), and its eligibility for grants is based on an assessment of the risk of debt distress. Countries with low risk of debt distress receive 100 percent of their IDA allocation as development credits. Countries with medium risk of debt distress receive 50 percent of their IDA allocation as development credits, and the other 50 percent as grants. Countries with high risk of debt distress will receive 100 percent of their allocation in the form of grants.

During FY2009, the first year of IDA15, total grants approved were \$2,575 million representing 18% of the total commitments of credits and grants of \$14,041 million.

4.3 Partial Risk Guarantees

In FY2009, IDA's Executive Directors approved the mainstreaming of the guarantees program, thereby ending the pilot status of the IDA guarantee program. Management maintains a program ceiling for IDA guarantees for risk management purposes, initially set at \$1.5 billion.

Instrument Type and Project Eligibility

IDA offers partial risk guarantees to cover private lenders or investors through shareholder loans, against the risk of a government (or government-owned entity) failing to perform its contractual obligations with respect to a private project, and where official agencies and the private market currently offer insufficient insurance coverage.

Partial risk guarantees can cover a range of sovereign or parastatal risks, subject to specific obligations contractually agreed to by the government for a specific project. The types of risks covered may vary, including but not limited to: (i) breach of contract; (ii) currency non-convertibility and non-transferability; (iii) changes in law; and (iv) expropriation and nationalization.

Table 4: Summary of Repayment Terms by Eligibility Criteria for Development Credits

Eligibility	Criteria	Repayment Terms
IDA Only	Not considered sufficiently creditworthy to borrow from IBRD. For FY2009, "IDA-only" borrowers had a 2007 GNI per capita of \$1,095 or less (the 'operational' cutoff)	40 years including a grace period of 10 years
Blend	May receive both IDA and IBRD financing. Blend borrowers have limited IBRD creditworthiness and a per capita GNI between \$730 and \$5,530	35 years including a grace period of 10 years
Hardened Terms	If a borrower's GNI per capita exceeds the operational cutoff for more than two consecutive years, IDA credits are extended on hardened terms	20 years including a grace period of 10 years
Hard-terms	A blend country will be eligible for an additional window of IDA lending at hard terms if its GNI per capita is below the operational cutoff and if it has an active IBRD lending program. Eligibility will be determined annually	35 years including a grace period of 10 years

In terms of project eligibility, guarantees are available in selective cases in IDA-only countries where an IBRD Enclave Guarantee² is not applicable and in blend countries which do not have access to IBRD funding due to creditworthiness constraints.

Guarantee Pricing

Standard charges consist of an annual *guarantee fee* of 0.75 percent on IDA's maximum exposure³ under the guarantee and an annual *standby fee or commitment* charge which is set to match the level of commitment charges applicable for IDA credits at the time of guarantee approval. The guarantee fee and the standby fee are payable either periodically in installments or in a single upfront payment, on a present-value basis. In addition, IDA charges a one-time initiation fee of 0.15 percent or \$100,000 (whichever is higher) and a processing fee of up to 0.50 percent of the principal amount of the guarantee for all private sector borrowers. The processing fee is determined on a case-by-case basis and can either be waived or increased in exceptional cases.

Counter-guarantee from the Government

When IDA issues a guarantee, it obtains a counter-guarantee from the host government. If the guarantee is called, IDA pays the project lenders. Without limiting its rights under the counter-guarantee (indemnity) agreement, IDA takes into account all relevant circumstances in deciding whether or not to exercise its right to demand compensation from the host government under the counter-guarantee, and what form the compensation

will take (for example whether it will be a cash settlement or converted into a credit to be repaid over time).

Guarantees Exposure

IDA's exposure on its guarantees (measured by discounting each guaranteed amount from its first call date) is \$198 million at June 30, 2009 (\$209 million at June 30, 2008). For additional information see the Notes to Financial Statements—Note D—Development Credits and Guarantees.

During the fiscal years ended June 30, 2009 and June 30, 2008, no guarantees provided by IDA were called.

4.4 Heavily Indebted Poor Countries (HIPC) Debt Initiative

The HIPC Debt Initiative is a comprehensive approach to reduce the external debt of the world's poorest, most heavily indebted countries, and it represented an important step forward in placing debt relief within an overall framework of poverty reduction. The countries that qualify for HIPC assistance are the poorest countries that are eligible for highly concessional assistance from IDA and from the IMF's Poverty Reduction and Growth Facility.

Implementation mechanisms of the Enhanced HIPC Framework include: (i) partial forgiveness of IDA debt service as it comes due, and (ii) in the case of countries with a substantial amount of outstanding IBRD debt, partial refinancing by IDA resources (excluding transfers from IBRD) of outstanding IBRD debt.

² IBRD Enclave Guarantees are partial risk guarantees structured for export-oriented commercial projects in IDA-only countries that generate foreign exchange.

³ IDA's maximum exposure to a borrower's risk under a guarantee is defined in a manner similar to disbursed credits, i.e., as the full value of the disbursed and outstanding balance under the guarantee financing.

Table 5: Status of countries under Enhanced HIPC Framework

Pre-Decision Point 4 countries	Eritrea, Somalia, Sudan, Union of the Comoros
Decision Point 9 countries	Afghanistan, Côte d'Ivoire, Chad, Democratic Republic of Congo, Guinea, Guinea-Bissau, Liberia, Republic of Congo, Togo
Completion Point 26 countries	Benin, Bolivia, Burkina Faso, Burundi, Cameroon, Central African Republic, Ethiopia, The Gambia, Ghana, Guyana, Haiti, Honduras, Madagascar, Malawi, Mali, Mauritania, Mozambique, Nicaragua, Niger, Rwanda, São Tomé and Príncipe, Senegal, Sierra Leone, Tanzania, Uganda, Zambia

The list of countries potentially eligible under the Enhanced HIPC Framework has been limited whereby no new countries can be considered for eligibility. As of June 30, 2009, the status of all potentially eligible and current HIPC countries according to stage reached under the Enhanced HIPC Framework is provided in **Table 5**.

As of June 30, 2009, the accumulated provision for HIPC Debt Initiative stands at \$3,251 million (\$4,215 million—June 30, 2008). The decrease of \$964 million was due to a combination of providing debt relief during the course of the year, Nepal's decision not to seek eligibility under the HIPC Debt Relief Initiative, credits being written off upon Burundi reaching its **completion point** and revisions of estimates due to **completion Point** dates being postponed for a number of countries.

4.5 Multilateral Debt Relief Initiative (MDRI)

The MDRI, approved by the Executive Directors in June 2006, provides additional debt relief through 100 percent cancellation of eligible debt owed to IDA, the African Development Bank and the International Monetary Fund by countries that reach the HIPC **completion point**. The objectives of MDRI are twofold: deepening debt relief to HIPC countries while safeguarding the long-term financial capacity of IDA and other participating multilateral institutions; and encouraging the best use of additional donor resources for development, by allocating them to low-income countries on the basis of policy performance.

Donors have agreed to compensate IDA on a dollar-for-dollar basis for forgone credit reflows due to debt cancellation under the MDRI. These resources are accounted for as subscriptions and contributions. As of June 30, 2009, IDA has received donor commitments to the MDRI in the amount of \$32,390 million at the agreed **replenishment** foreign exchange reference rates, representing 86% of the total financing requirements based on the updated cost estimates for the MDRI as of September 30, 2007. A summary by donor country of the **IoCs** received under the MDRI resolution as of June 30, 2009 is provided in Notes to Financial Statements – Note B – Members' Subscriptions and Contributions.

IDA provides in full for the estimated probable write-off of the principal component of debt relief to be delivered under the MDRI. As of June 30, 2009 the accumulated provision for MDRI is \$6,086 million (\$7,628 million, June 30, 2008). The decrease of \$1,542 million was due to a combination of Nepal's decision not to seek eligibility under the HIPC Debt Relief Initiative, credits being written off upon Burundi reaching its **completion point** and revisions of estimates due to **completion point** dates being postponed for a number of countries.

A list of development credits written off, by country, on an accumulated basis since implementation of the MDRI, commencing on July 1, 2006, is provided in the Notes to Financial Statements—Note D—Development Credits and Guarantees.

4.6 Financial Crisis Response Fast Track Facility

In December 2008, the Executive Directors approved the establishment of the **IDA Financial Crisis Response Fast-Track Facility** through which a better response can be provided against the impact of the global financial crisis on IDA countries by fostering a more responsive analysis of pressing needs of IDA borrowers, and a larger and faster response to those needs. The main parameters of this fast track facility are:

- An initial \$2 billion of IDA15 resources to be fast tracked from existing country allocations without any additional resources being provided under this Facility.
- Front loading or acceleration of commitments is allowed up to 50 percent in cases where fast-tracked operations cause annual country allocations to be exceeded.
- IDA-only and blend countries that can demonstrate a significant impact from the crisis are eligible.
- Fast track procedures include shortened management review periods.

Incremental demand for IDA's resources in response to the financial crisis has been limited to

date, but is expected to increase. As of June 30, 2009, ten operations totaling \$990 million and covering eight countries have been brought forward for fast track processing.

Section 5: FINANCIAL RESOURCES

5.1 Commitment Authority Framework

The resources available to IDA for funding its lending activities constitute its **commitment authority**. IDA finances its credit, guarantee and grant commitments primarily from subscriptions and contributions from donor countries. Additional funds come from IDA's internal resources, including reflows (repayments of principal on outstanding credits), investment income, and transfers by IBRD out of its net income and grants as designations out of IFC retained earnings. Since IDA's lending is highly concessional, its resources are periodically replenished, normally every three years. Since its inception, IDA's resources have been replenished fifteen times, complemented by an additional **replenishment** agreed in 2006 for financing the MDRI.

Starting from FY1989, the Executive Directors authorized IDA to make advance commitments against future reflows and other internal resources. The *Advance Commitment Scheme*⁴ was established in recognition of the fact that credits disburse over several years and therefore cash in hand is not needed at the time of commitment.⁵

5.2 Donor Resources

Replenishment Process

Donors normally replenish IDA's resources every three years. The regular **replenishment** process has several steps:

- (a) **Replenishment Discussions**. These include meetings between IDA's management and donor country representatives, called IDA **Deputies**. Issues discussed include the size of the **replenishment**, relative burden-sharing among donors, and the policy framework for the **replenishment**. Discussions in IDA15 included the issues of IDA's role in the global aid architecture; IDA's effectiveness at the country level; and IDA's support for fragile states. Contributions are negotiated in **SDR**

⁴ Credits, which disburse over several years, do not have to be fully cash funded at the time of their approval by the Executive Directors. This allows donor contributions to be encashed over several years and internal resources to be committed in advance of their anticipated receipt.

⁵ To determine the appropriate level of internal resources during a replenishment period, long-term financial projections are used to manage IDA's cash flows on a going concern basis, under a set of underlying assumptions relating to future lending volumes and the level of future donor contributions.

terms, and translated into national currencies using an average exchange rate, agreed upon early in the **replenishment** process.

- (b) **Advance Contributions Scheme**. To avoid disruption to IDA programs at the start of a new **replenishment**, donors can participate in an advance contributions scheme. The advance contributions scheme allows IDA to continue making new lending commitments without waiting for the new **replenishment** to become effective. The advance contribution scheme lapses once the new **replenishment** becomes effective. Donors can choose not to participate in the Advance Contribution Scheme.
- (c) **Replenishment Effectiveness**. The effective date of a **replenishment** occurs when IDA receives **Instruments of Commitment (IoCs)** from donors whose aggregate contributions account for not less than the amount defined in the Replenishment Resolution. IDA15 became effective on November 6, 2008, following the receipt of IoCs from donors above the minimum threshold of SDR 9,696 million set in the IDA15 Replenishment Resolution.
- (d) **Commitment Authority**. Donor contributions become available for commitment in three equal tranches. The first tranche becomes available for commitment upon the effectiveness of the advance contributions scheme or of the **replenishment**. The second and third tranches are subsequently released for commitment on the dates specified in the Replenishment Resolution.
- (e) **Payment of Contributions**. Typically, contributions are made in cash or non-interest bearing demand notes, on specified dates in three equal annual installments. A discount may be provided for cash payments based on an accelerated schedule rather than the standard **replenishment** schedule. The amount of discount is calculated so that the net present value of cash payments made according to the revised schedule is equal to the net present value of the cash payments under the **encashment** schedule agreed for the **replenishment**.
- (f) **Encashment**. Donor contributions are drawn down, on an approximately *pro rata* basis among donors, in accordance with the agreed **encashment** schedule.

Members' Voting Rights

IDA allocates votes to its members in two ways. **Membership votes** are allocated equally among members, and **subscription votes** are allocated in relation to a member's initial and subsequent subscriptions and contributions. The key rules governing the **voting rights** system are as follows:

- The voting power of each **Part I member** reflects its share of total cumulative financial contributions to IDA by all **Part I members**, plus its original **membership votes**;
- **Part II members** can maintain their relative voting power by making subscriptions at nominal cost⁶ and in national currency; and
- **Part II members** providing IDA with additional resources "in usable form"⁷ receive the same increase in voting power that **Part I members** receive for their contributions. After donor negotiations for a **replenishment** are completed, subscriptions are allocated to non-donor **Part II members** to provide them the opportunity to maintain their relative voting power.

Both Part I and II members receive additional **membership votes** when they make additional subscriptions. The distribution of **membership votes** helps smaller members and the **Part II members** as a group, to maintain their relative voting power.

Risks Associated with Donor Resources

IDA experiences foreign currency exposure due to currency mismatches between its disbursement obligations for credits and grants denominated in **SDR** and donor contributions denominated in national currencies. Exchange rate fluctuations will alter the **SDR** value of donor contributions from the time of commitment by donors until the actual **encashment** of these contributions. This currency risk is addressed in **Section 8.4 Market Risk**.

Delays in the timing of **encashment** affect IDA's liquidity. If **encashment** delays occur, IDA may agree with the donor on a revised **encashment** schedule that yields at least an equivalent value. Another risk is the potential for delays in declaring

effectiveness of the **replenishment** due to a delay in receipt of **Instruments of Commitment (IoCs)**.

5.3 Internal Resources

IDA's internal resources include reflows (principal repayments and income from charges less administrative expenses), investment income, the stock of liquidity, and residual resources from past **replenishments** that become available to IDA during the **replenishment** period. Repayments of outstanding credits constitute the largest component of internal resources.

Risks Associated with Internal Resources

Under the Advance Commitment Scheme, IDA makes commitments against projected levels of internal resources over the disbursement period of these commitments. The level of reflows would be affected if borrowers were to fall behind in their debt service. Reflows are also affected by the delivery of debt relief under HIPC and MDRI. Furthermore, the level of investment income varies with movements in market interest rates. It is therefore essential to ensure that resources are available to fund disbursements when they are needed. To monitor this risk, IDA's management reviews the level of **commitment authority** regularly and provides an annual report to IDA's Executive Directors.

5.4 IBRD Transfers

Since 1964, IDA has received regular financial support from IBRD in the form of annual direct transfers. By the end of FY2008 and coinciding with the end of IDA14, the total direct transfers received stood at \$9,845 million. The IDA15 financing framework includes an indicative amount of IBRD transfers of \$1,750 million. Dependent first on IBRD fulfilling its reserve retention needs, it is expected that this amount will be allocated in three installments during fiscal years 2009, 2010 and 2011. Each installment is required to be approved annually by IBRD's Board of Governors. If approved each installment is expected to be drawn down immediately. During FY2009, IDA received the first of these installments of \$583 million from IBRD, resulting in a cumulative direct transfer of \$10,428 million. In the context of the debt relief costs associated with the HIPC Debt Initiative, IBRD has provided additional resources to IDA through contributions to the Debt Relief Trust Fund totaling \$2,330 million as of June 30, 2009.

5.5 IFC Grants

Starting in 2006, IFC designated \$150 million out of its retained earnings as a grant to IDA. The IDA15 financing framework includes an indicative amount of \$1,750 million as grants to IDA. Of the

6 The nominal cost of one subscription vote was set at U.S.\$ 80 (1960 gold dollars) for the third replenishment, and U.S.\$ 25 (current dollars) in the subsequent replenishments. The effective cost of a vote for Part I members has grown from about \$9,900 under the third replenishment to about \$16,800 under the fifteenth replenishment.

7 Resources are deemed to be "in usable form" if they are provided in "freely convertible currency" as defined in Article 2, Section 2(f) of IDA's Articles of Agreement or in local currency available for financing in the donor country.

IDA15 indicative amount, IDA has already received \$950 million, resulting in cumulative grants received of \$1,100 million as of June 30, 2009. The remaining \$800 million is expected to be paid over FY2010 and FY2011, subject to availability of funds and would be paid immediately upon IDA and IFC signing the respective grant agreements. The proceeds of these IFC grants must be used by IDA for sectors and themes which contribute significantly to private sector growth and economic development in countries that are members of both IFC and IDA.

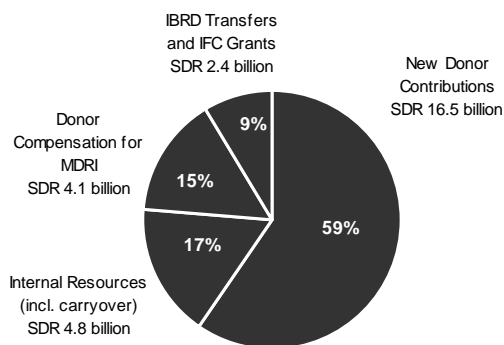
5.6 Other Transfers

Under agreements governing the administration of certain trust funds, IDA may receive surplus assets as transfers upon the termination of these trust funds. In addition, as development credits are repaid to trust funds, in certain cases the repaid funds are transferred to IDA. Receipts of these transfers are reported as income in the period in which they are received. Given the small size and the unpredictable timing of these transfers, they have not been included as part of any **replenishment** resources. However, these transfers have added to IDA's liquidity. Details of these transfers by transferee are provided in the Notes to Financial Statements—Note H—Trust Fund Administration

5.7 Fifteenth Replenishment of IDA's Resources (IDA15)

IDA15 runs from July 1, 2008 to June 30, 2011. **Chart 3** provides a breakdown of the principal sources making up the total lending envelope of SDR 27.8 billion under the IDA15 **Commitment Authority** Framework. Out of this total, SDR 8.4 billion (30%) was committed during the fiscal year ended June 30, 2009, leaving SDR 19.4 billion for future commitments during FY2010 and FY2011.

Chart 3: IDA15 Commitment Authority by Source of Funds



Total Lending Envelope of SDR 27.8 billion

Section 6 ALLOCATION OF RESOURCES

6.1 Performance Based Allocation System

A key concern for IDA is inequitable allocation of resources to borrowers given that special priorities of poverty reduction may be in force during a particular **replenishment** period. This risk of inequitable allocation is managed by allocating resources to borrowers based on a Performance Based Allocation (PBA) system (see **Chart 4**). The PBA system has evolved over time with modifications and enhancements being incorporated at successive **replenishments**. The performance-based allocations for all countries include a basic allocation of SDR4.5 million per country per **replenishment** (or SDR1.5 million annually), which benefits small states in particular.

6.2 Country Performance Rating

Under the PBA system individual country allocations are derived substantially from Country Performance Ratings (CPR), population and, to a lesser extent, GNI per capita.

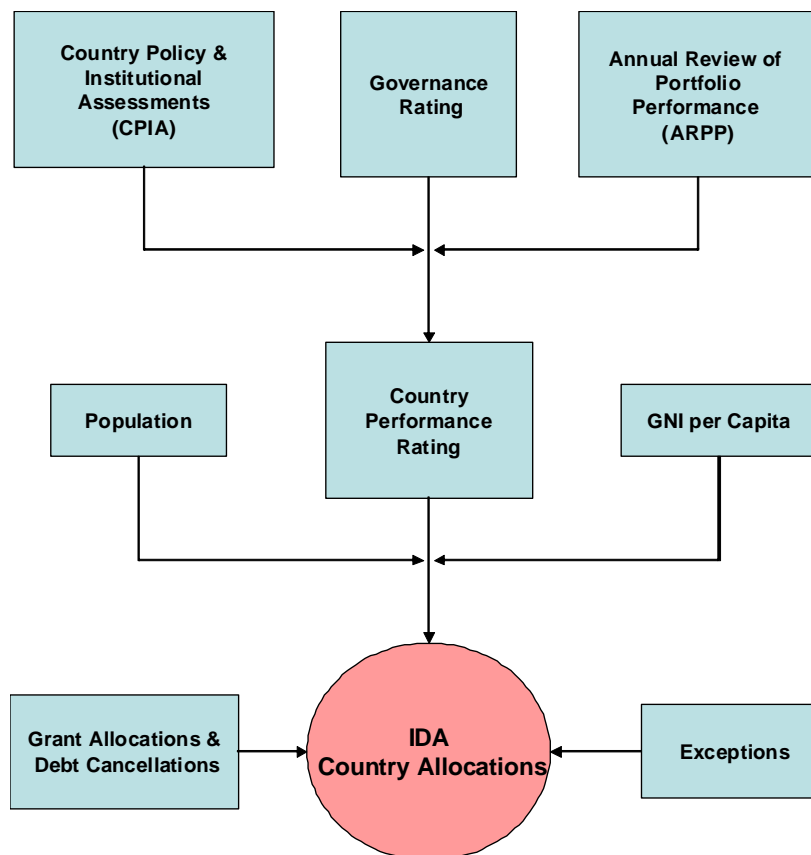
The Country Performance Ratings are assessed annually using a weighted combination of three elements:

- Country Policy and Institutional Assessments (CPIA), conducted annually by IDA to assess the quality of each country's policy and institutions for fostering sustainable growth, poverty reduction, and ability to effectively use development assistance. The CPIA assesses each country's policy and institutional framework and consists of defined criteria grouped into four equally weighted clusters: (A) economic management; (B) structural policies; (C) policies for social inclusion and equity; and (D) public sector management and institutions.
- The Annual Review of Portfolio Performance (ARPP), which captures the effectiveness of IDA-financed projects and programs based on the percentage of actual IDA problem projects in a given country.
- The Governance rating is calculated based on a review of public sector management and institutions.

6.3 Grant Allocations and Debt Cancellation

Before arriving at a country's final allocation, any grant allocations to that country are discounted. In addition, for those countries eligible for debt cancellation under the MDRI, the debt service due in the relevant fiscal year is netted out from that year's allocation.

Chart 4: IDA's Performance Based Allocation System



6.4 Exceptions

A number of specific exceptions to the PBA system have been agreed upon. These include:

- Capped-blend countries with access, or potential access to IBRD loans receive less than their allocation norms due to their broader financing options.
- Countries emerging from severe conflict can, under certain conditions, be provided with additional resources in support of their recovery and in recognition of a period of exceptional need.
- Additional allocations may be provided to IDA countries in the aftermath of major natural disasters, where the existing allocations would not allow for a sufficient response.

6.5 IDA15 Policy Framework

During the IDA15 period, IDA will be guided by the policy framework outlined in **Box 2**. This policy framework was agreed upon during the **replenishment** discussions.

Section 7: MANAGEMENT OF LIQUID ASSET HOLDINGS

7.1 Investment Policy Objectives

IDA is not a market-based financial entity, and in the absence of access to borrowed funds, IDA's primary objective in the management of its liquid assets is to ensure that funds will be available on a timely basis in the amount needed to meet future cash flow requirements, including disbursements for credits, grants and administrative expenses. Consistent with the primary objective, IDA also seeks to maximize returns, subject to loss constraints, to generate investment income, which can be added to IDA's internal resources.

7.2 Minimum Liquidity Levels

IDA is authorized to borrow from the capital markets under its Articles of Agreement. However, IDA does not borrow as a matter of policy, other than for short-term cash management purposes. During the IDA15 period, fiscal year 2009 to 2011, IDA's minimum liquidity is set at 33 percent of a three-year annual moving average of gross disbursements. IDA's minimum liquidity is designed to meet both expected and unexpected demands.

Box 2: IDA15 Policy Framework

- A. Reinforcing IDA's pivotal role in the global aid architecture
 - Scaling up regional projects especially those located in Sub-Saharan Africa
 - Paying more attention to the interplay between vertical funds and the country based models.
 - Mainstreaming climate change actions into its Country Assistance Strategies particularly in adaptation and access to clean energy.
 - Continue strengthening the application of the Debt Sustainability Framework and its use as the primary basis for grant allocation during IDA 15.
 - Continuing with the use of country-specific debt distress risk ratings in determining the mix of grants and credits for IDA-only countries.
 - Accelerating efforts in building debt management capacity in IDA-eligible countries.
 - Strengthening the tracking of progress on gender outcomes.
- B. Enhancing country-level effectiveness in ensuring progress towards the Millennium Development Goals
 - Simplifying the Performance-Based Allocation formula and reducing volatility in allocating IDA resources.
 - Updating the study of links between aid allocation and results, including the experience with Performance-Based Allocation and Country Policy and Institutional Assessment Ratings.
 - Continue improvement with the Results Measurement System, which has strengthened focus on results at the country level.
 - Strengthening statistical capacity in IDA countries.
 - Accelerate progress in its implementation of the Paris Declaration on Aid Effectiveness, especially on harmonization and alignment.
- C. Strengthening effectiveness in fragile states
 - Adaptation of Country Assistance Strategies to fragile and conflict-affected environments and developing better indicators on state-building and peace-building activities in fragile states.
 - Strengthening financial assistance to post-conflict and re engaging countries by lengthening the duration of exceptional assistance.
 - Continue calibrating IDA's financial assistance to post-conflict and re-engaging countries based on performance as measured by the Post-Conflict Performance Indicators.

Based on an analysis of expected and unexpected demands, IDA's low case minimum liquidity requirement has been estimated at around \$3.5 billion at present with the high case defined as 150 percent of the low case amount.

7.3 General Investment Authorization

The General Investment Authorization for IDA approved by the Executive Directors provides the basic authority under which the liquid assets of IDA can be invested. Further, all investment activities are conducted in accordance with a more detailed set of Investment Guidelines. The Investment Guidelines are approved by the Chief Financial Officer and implemented by the Treasurer. These Investment Guidelines set out detailed trading and operational rules including providing criteria for eligible instruments for investment, establishing risk parameters relative to benchmarks, such as an overall **stop-loss** limit and **duration** deviation, specifying concentration limits on counterparties and instrument classes, as well as establishing clear lines of responsibility for risk monitoring and compliance.

7.4 Liquidity Tranching

Starting in FY2009, IDA's liquid assets are invested in three separate tranches as described below.

Tranche 1 This tranche includes balances of accelerated **encashment** of donor contributions and transfers and grants from IBRD and IFC. The benchmark of this tranche is designed to be **duration** neutral in comparison to the stream of future net cash outflows such that the variation in investment earnings will be largely matched by equivalent changes in the present value of contractual net cash outflows of IDA. The **duration** is periodically reviewed and reset at least annually to reflect the **duration** of the future net cash outflows as well as prevailing market conditions.

Tranche 2 This is a medium term investment tranche and includes liquidity required to fund commitments of development credits and grants and a portion of the minimum liquidity. This tranche is

managed in accordance with a return maximization strategy subject to pre-specified risk constraints over a medium-term (three year) investment horizon. The **duration** and associated benchmarks of this tranche are reviewed and adjusted periodically as needed, in line with market conditions so as to conform to the specified risk tolerance.

Tranche 3 This is a short-term investment tranche and includes liquidity needed for IDA's ongoing financial operations with an investment horizon of less than one year. The tranche is comprised primarily of working capital needed for the current year and a portion of the minimum liquidity. The paramount investment objective of this tranche is to ensure liquidity and timely availability of the investment balances when needed, with investment returns being a secondary consideration. The tranche is invested in the form of overnight and very short-term cash investments.

Prior to FY2009, the liquid assets were invested in two tranches.

A reconciliation of the Net Investment Portfolio to the line items appearing on the Balance Sheet is provided in Note C—Investments of IDA's Financial Statements. This note also provides the currency composition of the Net Investment Portfolio, which shows that the investments are denominated in the composite currencies of the **SDR**. IDA's Net Investment Portfolio combining all the three tranches was \$21,287 million at June 30, 2009 (\$19,053 million—June 30, 2008).

Section 8: FINANCIAL RISK MANAGEMENT

IDA assumes various kinds of risk in the process of providing concessional financing. Its activities can give rise to four major types of risk: credit risk; market risk (interest rate and exchange rate); liquidity risk; and operational risk. The major inherent risk to IDA is country credit risk.

8.1 Governance Structure

A Risk Management governance structure supports Senior Management in their oversight function, particularly in the coordination of different aspects of risk management, and in connection with risks that cut across functional areas.

The Finance Committee, chaired by the Chief Financial Officer, makes recommendations and, where appropriate takes decisions in the areas of financial policy and oversight of financial reporting. The subcommittees that report to the Finance Committee are the Strategy, Performance and Risk

Subcommittee, the Credit Risk Subcommittee and the Finance Initiatives Subcommittee.

The Strategy, Performance and Risk Subcommittee develops and monitors the policies under which market and commercial credit risks faced by IDA are measured, reported and managed. The Subcommittee also monitors compliance with policies governing commercial credit exposure and currency management. Specific areas of activity include reviewing and endorsing guidelines for limiting balance sheet and market risks, the use of derivative instruments, investing activities, and monitoring matches between assets and their funding. In addition, the Subcommittee meets quarterly to formally review current and proposed business strategy and risk limits/policies, along with business results, and financial risk profile to facilitate alignment between business and risk management. The Credit Risk Subcommittee monitors the measurement and reporting of country credit risk and reviews the impact on the provision for losses on development credits and guarantees of any changes in exposure, risk ratings of borrowing member countries, or movements between the accrual and nonaccrual portfolios. The Finance Initiatives Subcommittee reviews the financial, organizational and implementation implications of new initiatives that may impact IDA.

The IDA Resource Mobilization Department which reports to the Vice President of Concessional Finance and Global Partnerships, manages IDA **replenishments**. This department discusses policy and funding frameworks with donors, and allocates concessional resources. Responsibility for financial management, including asset-liability management and the management of liquidity, currency and interest rate risks, also lies with this department.

Country credit risk, the primary risk faced by IDA, is identified, measured and monitored by the Credit Risk Department, led by the Chief Credit Officer who reports to the Vice-President, Corporate Finance and Risk Management. This unit is independent from IDA's operational business units.

Moreover, in order to further protect the independence of the unit, individual country credit risk ratings are not shared with the Executive Directors and are not made public. In addition, this department is responsible for determining the adequacy of provisions for losses on credits and guarantees and monitoring borrowers that are vulnerable to crises in the near term.

Counterparty credit risks in IDA's financial operations are identified, measured and monitored by the Corporate Finance Department, which also reports to the Vice-President, Corporate Finance and Risk Management. The Corporate Finance

Department works with IDA's financial managers, who are responsible for the day-to-day management of these risks, to establish and document processes that facilitate, control and monitor risk. These processes are built on a foundation of initial identification and measurement of risks by each of the business units. Under the direction of the Finance Committee, policies and procedures for measuring and managing such risks are formulated, approved and communicated throughout IDA. Senior managers represented on the Committee are responsible for maintaining sound credit assessments, addressing transaction and product risk issues, providing an independent review function and monitoring the development credits and investments.

The primary responsibility for the management of operational risk in IDA's financial operations resides with each of IDA's managers. These individuals are responsible for identifying operational risks and establishing, maintaining and monitoring appropriate internal controls in their respective areas using an operational risk management framework.

This framework requires each business unit to document operational risks and controls, assess the likelihood and impact of operational risks and evaluate the design and operating effectiveness of existing controls using guidelines established by IDA. An independent operational risk control unit supports this process by undertaking periodic reviews, performing quality assurance testing and reporting exceptions.

The processes and procedures by which IDA manages its risk profile continually evolve as its activities change in response to market, credit, product, operational and other developments. The Executive Directors, particularly the Audit Committee members, periodically review trends in IDA's risk profiles and performance, as well as any significant developments in risk management policies and controls.

8.2 Managing Risk Bearing Capacity

The risk bearing capacity of IDA falls under two main categories. The first is the extent to which IDA can commit to new financing of credits, grants and guarantees given its financial position at any point in time. The second is whether IDA has sufficient liquidity to meet temporary demands due to expected volatility in cash inflows and outflows, and unexpected net draw-downs of liquid resources, which would not be reversed over time.

Capacity to commit to new financing of credits and grants.

IDA's capacity to commit to new financing of credits and grants at any point in time is defined by the **Commitment Authority** Framework of the particular **replenishment** which is effective at that time. The risks to this lending capacity can arise from both donor and internal resources. These risks are discussed in **Section 5 Financial Resources**.

Sufficient liquidity to meet both expected and unexpected demands

Based on estimates of liquidity demand (see **Section 7 Management of Liquid Asset Holdings**) IDA's minimum liquidity requirement has been estimated within a band of \$3.5 billion to \$5.25 billion. During FY2009, the actual minimum liquidity and the unrestricted currency balances due from banks did not fall below \$3.5 billion.

8.3 Credit Risk

Country Credit Risk

Country risk is the risk of loss due to a borrowing member country not meeting its contractual payment obligations. The IDA Resource Mobilization Department regularly reviews the credit risk of its borrowing member countries in terms of the country's debt sustaining capacity, in conjunction with the Credit Risk Department. These reviews provide an input in determining the allocation of **commitment authority** resources for a borrowing member country as well as the composition of credits versus grants for new operations. **Section 4.2 Development Grants** describes how funds are allocated for grants based on a country's risk of debt distress.

Overdue and non-performing credits

When a borrower fails to make payment on any principal, interest or other charges, IDA has the contractual right to suspend disbursements immediately on all credits and grants. IDA's current policy however, is to exercise this right through a graduated approach as summarized in **Box 3**. These policies also apply to those member countries who are eligible to borrow from both IBRD and IDA, and whose payments on IBRD loans may become overdue. For borrowers with IDA credits who become overdue in their debt service payments on IBRD loans, IDA also applies the treatment described in **Box 3**. For a summary of countries with credits or guarantees in nonaccrual status at June 30, 2009, see Notes to Financial Statements–Note D–Development Credits and Guarantees

Box 3: Treatment of Overdue Payments

Overdue by 30 days	Where the borrower is the member country, no new development credits or grants to the member country, or to any other borrower in the country, will be presented to the Board of Executive Directors for approval; nor will any previously approved credits or grants be signed, until payments for all amounts 30 days overdue or longer have been received. Where the borrower is not the member country, no new credits or grants to that borrower will be signed or approved.
Overdue by 45 days	In addition to the provisions cited above for payments overdue by 30 days, to avoid proceeding further on the notification process leading to suspension of disbursements, the country as borrower or guarantor and all borrowers in the country must pay not only all payments overdue by 30 days or more, but also all payments due regardless of the number of days since they have fallen due. Where the borrower is not the member country, no new development credits or grants to, or guaranteed by, the member country, will be signed or approved.
Overdue by 60 days	In addition to the suspension of approval for new development credits or grants and signing of previously approved credits or grants, disbursements on all grants or credits to or guaranteed by the member country are suspended until all overdue amounts have been paid. This policy applies even when the borrower is not the member country. Under exceptional circumstances, disbursements could be made to a member country upon approval by the Executive Directors.
Overdue by more than six months	All development credits made to or guaranteed by a member of IDA are placed in nonaccrual status, unless IDA determines that the overdue amount will be collected in the immediate future. Unpaid service charges and other charges not yet paid on development credits outstanding are deducted from the income of the current period. To the extent that these payments are received, they are included in income. At the time of arrears clearance, a decision is made on the restoration of accrual status on a case-by-case basis; in certain cases that decision may be deferred until after a suitable period of payment performance has passed.

Accumulated Provision for HIPC Debt Initiative and MDRI

The adequacy of the accumulated provision for debt relief for the HIPC Debt Initiative and MDRI is based on both quantitative and qualitative analyses of various factors, including estimates of decision and **completion point** dates. IDA periodically reviews these factors and reassesses the adequacy of the accumulated provision for the HIPC Debt Initiative and MDRI. Adjustments to the accumulated provision are recorded as a charge against or addition to income. The methodology for determining the accumulated provision for losses under the HIPC Debt Initiative and MDRI is discussed in **Section 9, Critical Accounting Policies**.

Accumulated Provision for Losses on Development Credits and Guarantees

Delays in receiving payments from development credits or guarantee premiums result in present value losses to IDA since it does not charge fees or additional service charges or interest on any overdue service charges, interest or other charges. These present value losses are equal to the difference between the present value of payments of service charges and other charges made according to the credit's contractual terms and the present value of its expected future cash flows.

Management determines the appropriate level of accumulated provision for losses on credits and guarantees after taking into consideration the expected relief under the HIPC Debt Initiative and MDRI. This accumulated provision reflects the probable losses inherent in its nonaccrual and accrual portfolios. The methodology for determining the accumulated provision for losses on credits and guarantees is discussed in **Section 9, Critical Accounting Policies**.

The Credit Risk Subcommittee reviews the provision for losses on credits and guarantees at least quarterly and, if necessary, adjustments are made to the provision. In addition, the Audit Committee is apprised by management at least twice a year on the accumulated provision for losses on credits and guarantees.

The accumulated provision for losses on both the accrual and nonaccrual credit portfolio (excluding guarantees) decreased by \$13 million from \$1,253 million at June 30, 2008 to \$1,240 million at June 30 2009. This decrease comprises translation adjustment of \$42 million offset by an increase of provision for losses on credits of \$29 million. The increase of provision for losses on credits was primarily due to changes in the volume and distribution of development credits outstanding, partially offset by the net impact of changes in the credit quality of the development credit portfolio,

and the annual update of the expected default frequencies (probability of default to IDA).

Commercial Credit Risk

Commercial credit risk is the risk of loss due to a counterparty not honoring its contractual obligations. IDA's commercial credit risk is concentrated in investments in debt instruments issued by sovereign governments, agencies, banks and corporate entities. The majority of these investments are in AAA and AA rated instruments.

In the normal course of its business, IDA utilizes various derivatives and foreign exchange financial instruments, to generate income through its investment activities and for asset/liability management purposes. Derivative and foreign exchange transactions also involve credit risk. The effective management of credit risk is vital to the success of IDA's investment and asset/liability management activities. The monitoring and managing of these risks is a continuous process due to changing market environments.

IDA controls the counterparty credit risk arising from investments, derivatives and asset/liability management activities through its credit approval process, and monitoring procedures. The credit approval process involves evaluating counterparty creditworthiness, assigning credit limits and determining the risk profile of specific transactions. Credit limits are calculated and monitored on the basis of potential exposures taking into consideration current market values and estimates of potential future movements in those values.

IDA measures the credit risk exposure as the replacement cost of the derivative or foreign exchange product. This is also referred to as replacement risk or the mark-to-market exposure amount. While notional principal is the most commonly used volume measure in the derivative and foreign exchange markets, it is not a measure of credit or market risk.

Mark-to-market exposure is a measure, at a point in time, of the value of a derivative or foreign exchange contract in the market. When the mark-to-market is positive, it indicates the counterparty owes IDA and, therefore, creates an exposure for IDA. When the mark-to-market is negative, IDA owes the counterparty and does not have replacement risk.

Table 6 provides details of IDA's estimated credit exposure on its investments and swaps, net of collateral held, by counterparty rating category. The most important development during FY2009 has been the shift towards AAA rated counterparties, from 51% to 66%. This flight to quality during the current turmoil in the financial markets was achieved by moving from banks to high-grade sovereigns, sovereign-guaranteed bank debt, and agencies which offer implicit government guarantees. Other developments included downgrades of a small portion of the holdings of **asset-backed securities (ABS)** due to mono-line insurers being downgraded. As a result the ratings for a small portion went down to CCC at June 30, 2009.

8.4 Market Risk

IDA faces risks which result from market movements, primarily changes in currency exchange and interest rates. The manner in which these market risks impact IDA's finances and the steps taken by IDA to counter them is described below.

Currency Risk

IDA faces currency risk exposure as a result of the currency mismatch between its commitments for development credits and grants, which are denominated in **SDRs**; donor contributions, which are denominated in both national currencies and SDRs; and the portion of IDA's internal resources and expenditures that is denominated in U.S. dollars.

Table 6: IDA Investment Credit Exposure, Net of Collateral Held, By Counterparty Rating

In millions of U.S. dollars

Counterparty Rating	At June 30, 2009				At June 30, 2008		
	Sovereigns	Agencies, ABS and Banks	Swaps	Total	% of Total	Total	% of Total
AAA	\$12,368	\$ 4,927	\$375	\$17,670	66	\$14,591	51
AA	2,749	3,799		6,548	24	14,252	49
A		2,612		2,612	10	71	*
BBB		5		5	*	3	*
BB		1		1	*	3	*
CCC		1		1	*		
Total	<u>\$15,117</u>	<u>\$11,345</u>	<u>\$375</u>	<u>\$26,837</u>	<u>100</u>	<u>\$28,920</u>	<u>100</u>

* Denotes less than 0.5%.

IDA mitigates this risk by adjusting the currency composition of its liquid asset portfolio through foreign exchange transactions.

Starting from May 2008, IDA extended its currency risk management tools to include the use of currency forward contracts to convert donors' **encashments** provided in national currencies into the four currencies of the **SDR** basket. IDA's transactions are intermediated by IBRD for efficiency purposes, due to IBRD's established systems and collateral management processes.

Under this arrangement, IDA enters into foreign exchange forwards with IBRD, and IBRD simultaneously enters into off-setting foreign exchange forwards with market counterparts. For further details please see Notes to Financial Statements-Note F-Derivative Instruments.

IDA funds a portion of its credits with internal resources, including investment income on its liquid asset portfolio. Details of the investment objectives of each of the three tranches of IDA's liquid assets are provided in **Section 7 – Management of Liquid Asset Holdings**.

8.5 Operational Risk

Operational risk is the potential for loss resulting from inadequate or failed internal processes or systems, human factors, or external events, and includes business disruption and system failure, transaction processing failures and failures in execution of legal, fiduciary and agency responsibilities. IDA, like all financial institutions, is exposed to many types of operational risks.

IDA attempts to mitigate operational risk by maintaining a system of internal controls that is designed to keep that risk at appropriate levels in view of the financial strength of IDA and the characteristics of the activities and markets in which IDA operates.

The operational risk management framework used by IDA is based on the Integrated Risk Management Framework approved by the Board in January 2003 and involves the following core steps:

- Key operational risks are identified annually and documented using a combination of tools including business process review and risk assessments.
- Operational risks are assessed based on likelihood of occurrence and the resulting financial impact using probability and severity parameters.
- Controls that mitigate operational risks are evaluated using a combination of processes including self assessment workshops, independent walk through tests of processes,

independent compliance testing by IDA's internal audit department, quality assurance testing by management, project reviews undertaken by the Independent Evaluation Group and annual internal representation letters from business unit managers.

- The results of the work undertaken to evaluate risks and operational effectiveness of internal controls are reported to the Audit Committee.

IDA Controls Review over Lending Operations

In FY2009, IDA completed a comprehensive and independent review of internal controls over lending operations to fulfill a commitment made to donors during the negotiations of IDA's fourteenth **replenishment**. This review used the rigorous **Committee of Sponsoring Organizations of the Treadway Commission (COSO)** framework and methodology, which establishes "a common definition of internal controls, standards, and criteria against which companies and organizations can assess their control systems." These control systems ensure that funds are used efficiently and for their intended purpose, and include procurement processes, supervision mechanisms and procedures and measures to prevent fraud and corruption. The review was in-depth and extensive, and encompassed three levels: (1) a management self-assessment of the control framework; (2) review by the Internal Auditing Department (IAD); and (3) independent evaluation by the Bank Group's Independent Evaluation Group (IEG).

The results of the IDA Controls Review have provided management and the Executive Directors with reasonable assurance that the three COSO objectives of (i) reliable financial reporting, (ii) compliance with policies and procedures, and (iii) the efficiency and effectiveness of operations, are being achieved subject to a number of qualifications. These qualifications which do not impact the reliability of internal controls over financial reporting, relate to issues in lending operations. To address these issues, management has adopted and begun implementing a detailed action plan. An independent Implementation Oversight Panel (IOP) has been established to monitor, oversee, and advise the President and the Executive Directors on the implementation status and progress achieved.

Internal Controls Over External Financial Reporting

Since FY1997, IDA's management has made an annual assertion that, as of June 30 of each fiscal year, its system of internal control over its external financial reporting has met the criteria for effective internal control over external financial reporting as described in the **COSO** framework. Concurrently

since FY1997, IDA's external auditors have provided an attestation report that management's assertion regarding the effectiveness of internal control over external financial reporting is fairly stated in all material respects.

Management has carried out an evaluation of internal control over external financial reporting for the purpose of determining if there were any changes made in internal controls during the fiscal year covered by this report that had materially affected, or would be reasonably likely to materially affect IDA's internal controls over external financial reporting. As of June 30, 2009 no such significant changes had occurred.

Section 9: CRITICAL ACCOUNTING POLICIES

The Notes to IDA's financial statements contain a summary of IDA's significant accounting policies. The following is a description of those accounting policies, which involve significant management judgments that are difficult, complex or subjective and relate to matters that are inherently uncertain.

9.1 Valuation of Financial Instruments

Derivative financial instruments and investment securities are recorded in IDA's financial statements at fair value. Disclosures related to the fair value of these, and other financial instruments are included in Note M – Fair Value of Financial Instruments. Fair value is based on market quotations when possible. Financial instruments for which market quotations are not readily available have been valued based on discounted cash flow models using market estimates of cash flows and discount rates. All the financial models used for input to IDA's financial statements are subject to both internal and periodic external verification and review by qualified personnel. These models use market sourced inputs, such as interest rates, exchange rates and volatilities. Selection of these inputs may involve some judgment. Imprecision in estimating these factors, and changes in assumptions, can impact net income and IDA's financial position as reported in the financial statements. IDA believes its estimates of fair value are reasonable given its processes for obtaining external prices and parameters, ensuring that valuation models are reviewed and validated both internally and externally, and applying its approach consistently from period to period.

9.2 Provision for HIPC Debt Initiative and MDRI

The adequacy of the accumulated provision for the HIPC Debt Initiative and MDRI is based on both quantitative and qualitative analyses of various factors, including estimates of decision and **completion point** dates. IDA periodically reviews these factors and reassesses the adequacy of the accumulated provision for the HIPC Debt Initiative

and MDRI. Adjustments to the accumulated provision are recorded as a charge against or addition to income.

9.3 Provision for Losses on Development Credits and Guarantees

IDA's accumulated provision for losses on credits and guarantees reflects the probable losses inherent in its nonaccrual and accrual portfolios after taking into consideration the expected relief under the HIPC Debt Initiative and MDRI. The provision required is a function of the expected default frequency and the assumed severity of the loss (given default) for each of the borrowers.

The expected default frequency has the borrower's risk rating assigned to it. The determination of a borrower's risk rating is based on both quantitative and qualitative analyses of various factors, which include political risk, external debt and liquidity, fiscal policy and public debt burden, balance of payments risks, economic structure and growth prospects, monetary and exchange rate policy, financial sector risks and corporate sector debt and other vulnerabilities. IDA periodically reviews such factors and reassesses the adequacy of the accumulated provision for losses on credits and guarantees accordingly. Adjustments to the accumulated provision are recorded as a charge against or addition to income. Actual losses may differ from expected losses due to unforeseen changes in any of the factors that affect borrowers' creditworthiness.

Additional information on IDA's provisioning policy and the status of nonaccrual loans can be found in the Notes to Financial Statements-Note A-Summary of Significant Accounting and Related Policies and Note D-Development Credits and Guarantees.

9.4 Pension and Other Postretirement Benefits

IBRD, IFC and MIGA participate in pension and postretirement benefit plans that cover substantially all of their staff members. All costs, assets and liabilities associated with the plans are allocated between IBRD, IFC and MIGA based upon their employees' respective participation in the plans. Costs allocated to IBRD are subsequently shared between IBRD and IDA based on an agreed cost sharing ratio. The underlying actuarial assumptions used to determine the projected benefit obligations, accumulated benefit obligations and funded status associated with these plans are based on financial market interest rates, past experience, and management's best estimate of future benefit changes and economic conditions. For further details, please refer to Notes to Financial Statements-Note L-Pension and Other Postretirement Benefits.

Section 10: GOVERNANCE

10.1 General Governance

IDA's decision-making structure consists of the Board of Governors, the Executive Directors (the Board) and the President and staff. The Board of Governors is the highest decision-making authority. The Board of Governors may delegate authority to the Board to exercise any of its powers, with the exception of certain powers enumerated in IDA's Articles of Agreement (Article VI, Section 2(c)).

The Board is responsible for IDA's general operations. It reviews and approves IDA's financial policies and practices, including:

- financial products and programs, such as the terms and conditions of development credits, grants and guarantees, and the provision and modalities of debt relief under the HIPC Debt Initiative; and
- financial management policies, such as investment authority and policy, the method of apportioning administrative expenses between IDA and IBRD, and the use of IDA's internal resources.

The President is the Chairman of the Board and chief of the operating staff of IDA. Under the direction of the Board, the President conducts the ordinary business of IDA and is responsible for the organization, appointment and dismissal of its officers and staff.

Management Changes

During FY 2009, Ms. Anne-Marie Leroy was appointed as Senior Vice President & World Bank Group General Counsel effective March 9, 2009.

Board Membership

In accordance with its Articles of Agreement, members of IDA's Executive Directors are appointed or elected by their member governments. These Executive Directors are neither officers nor staff of IDA. The President is the only management member of the Board of Executive Directors, serving as a non-voting member and as Chairman of the Board. The Executive Directors have established several Committees including:

- Audit Committee
- Budget Committee
- Committee on Development Effectiveness
- Committee on Governance and Administrative Matters
- Ethics Committee
- Personnel Committee

The Executive Directors and their Committees function in continuous session at the principal offices of IDA, as business requires. Each Committee's terms of reference establishes its respective roles and responsibilities. As Committees do not vote on issues, their role is primarily to serve the Board of Executive Directors in discharging its responsibilities.

10.2 Audit Committee

Membership

The Audit Committee consists of eight members drawn from the Board. Membership on the Committee is determined by the Board, based upon nominations by the Chairman of the Board, following informal consultation with the Executive Directors. In addition, membership of the Committee is expected to reflect the economic and geographic diversity of IDA's member countries and a balanced representation between borrowing and non-borrowing member countries. Generally, Committee members are appointed for a two year term; reappointment to a second term, when possible, is desirable for continuity. Audit Committee meetings are generally open to any member of the Board who may wish to attend, and non-Committee members of the Board may participate in the discussion. In addition, the Chairman of the Audit Committee may speak in that capacity at meetings of the Board, with respect to discussions held in the Audit Committee.

Key Responsibilities

The Audit Committee is appointed by the Board to assist it in the oversight and assessment of IDA's finances and accounting, including the effectiveness of financial policies, the integrity of financial statements, the system of internal controls regarding finance, accounting and ethics (including fraud and corruption), and financial and operational risks. The Audit Committee also has the responsibility for reviewing the performance and recommending to the Board the appointment of the external auditor, as well as monitoring the independence of the external auditor and meeting with it in executive session. The Audit Committee participates in oversight of the internal audit function, including reviewing the responsibilities, staffing and the effectiveness of internal audit. The Committee also reviews the annual internal audit plan and meets with the Auditor General in executive session. In the execution of its role, the Committee discusses with management, the external auditors, and the internal auditors, financial issues and policies which have a bearing on IDA's financial position. The Audit Committee monitors the evolution of developments in corporate governance and the role of audit

committees on an ongoing basis and updated its terms of reference in July 2009.

Communications

The Audit Committee communicates regularly with the full Board through distribution of the following:

- The minutes of its meetings.
- Reports of the Audit Committee prepared by its Chairman, which document discussions held. These reports are distributed to the Executive Directors, Alternates, World Bank Group Senior Management and Vice Presidents.
- “Statement(s) of the Chairman” and statements issued by other members of the Committee.
- The Annual Report to the Board of Executive Directors, which provides an overview of the main issues addressed by the Committee over the year.

The Audit Committee's communications with the external auditor are described in **Section 10.4 Auditor Independence**.

Executive Sessions

Members of the Committee may convene in executive session at any time, without management present. Under the Committee's terms of reference, it meets separately in executive session with the external and internal auditors.

Access to Resources and to Management

Throughout the year, the Audit Committee receives a large volume of information, which supports the preparation of the financial statements. The Audit Committee meets both formally and informally throughout the year to discuss financial and accounting matters. Executive Directors have complete access to management. The Audit Committee reviews and discusses with management the quarterly and annual financial statements. The Committee also reviews with the external auditor, the financial statements prior to their publication and recommends them for approval to the Board.

The Audit Committee has the capacity, under exceptional circumstances, to obtain advice and assistance from outside legal, accounting or other advisors as deemed appropriate.

10.3 Code of Conduct and Business Conduct Infrastructure

The World Bank Group promotes a positive work environment where staff members understand their ethical obligations to the institution, which are embodied in its Core Values and Principles of Staff Employment. In support of this commitment, the

institution has in place a Code of Professional Ethics, entitled *Living our Values*. The Code applies to all staff worldwide and is available on the World Bank's website, www.worldbank.org.

Orientation training for new staff and other ethics training, attended by approximately 3,000 staff annually, promote awareness and familiarize staff with the Code.

The World Bank Group is currently finalizing an updated Code, which is expected to be rolled out to staff in the first quarter FY 2010 as the “*Code of Conduct*.” An e-learning module on the updated Code is also in the final design phases, with rollout planned for the second quarter FY 2010. This training will be for certification, and staff, including consultants, will be required to complete an acknowledgment that they will abide by the tenets of the Code.

In addition to the Code, the business conduct obligations of staff are articulated in the Staff Manual (Principles of Staff Employment, Staff Rules), Administrative Manual and other guidelines. The Principles and Staff Rules require that all staff avoid or properly manage conflicts of interest. In accordance with the Staff Rules, senior managers must complete a confidential financial disclosure instrument with the Office of Ethics and Business Conduct.

In addition to the Code, rules and policies, guidance for staff is also provided through programs, training materials, and other resources. Managers are responsible for ensuring that internal systems, policies, and procedures are consistently aligned with the World Bank Group's business conduct framework.

The following World Bank Group units assist in communicating business conduct expectations to staff:

- The Office of Ethics and Business Conduct (EBC) works to ensure that staff are aware of their business conduct-related obligations. It provides insight on ethics trends to senior management and oversees related outreach, training and communication initiatives. EBC also handles allegations of staff misconduct not involving significant fraud and corruption.
- The Integrity Vice Presidency (INT) is charged with investigating allegations of significant fraud and corruption both within the World Bank Group and in Bank-funded projects worldwide. It also trains and educates staff and clients in detecting and reporting fraud and corruption.

Both EBC and INT report directly to the President of the World Bank Group. Staff from these units include professionals from a broad range of disciplines including trainers, financial analysts, researchers, investigators, lawyers, prosecutors, forensic accountants, and staff with World Bank Group operational experience. These units maintain comprehensive websites to provide guidance on how to handle concerns.

The World Bank Group has both an Ethics HelpLine and a Fraud and Corruption hotline, overseen by EBC and INT respectively. These resources are referenced in the Code, and are run by an outside firm staffed by trained specialists. This third-party service offers numerous methods of communication in addition to a toll free service in countries where access to telecommunications may be limited. These phone services can accept calls in multiple languages. Other reporting channels include: phone, mail, email (EBC maintains a Notes service account called Ethics Helpline), or through the units' respective websites. Callers may also visit the offices in person.

IDA has in place procedures for the receipt, retention and handling of recommendations and concerns identified during accounting, internal control and auditing processes.

The World Bank Group's Staff Rules clarify and codify the obligations of staff in reporting suspected fraud, corruption or other misconduct that may threaten the operations or governance of the Bank Group. Additionally, these rules offer protection from retaliation. In 2008, the institution implemented strengthened whistleblower protections.

10.4 Auditor Independence

In FY 2003, the Board adopted a set of principles applicable to the appointment of the external auditor for IDA. Key features of those principles include:

- Prohibition of the external auditor from the provision of all non audit-related services.
- All audit-related services must be pre-approved on a case-by-case basis by the Board, upon recommendation of the Audit Committee.
- Mandatory rebidding of the external audit contract every five years.
- Prohibition of any firm serving as external auditors for more than two consecutive five-year terms.
- Mandatory rotation of the senior partner after five years.

- An evaluation of the performance of the external auditor at the mid-point of the five year term.

External auditors are appointed to a five-year term of service. This is subject to annual reappointment based on the recommendation of the Audit Committee and approval of a resolution by the Executive Directors. In FY2009, KPMG began a five-year term as IDA's external auditor.

As a standard practice, the external auditor is present as an observer at virtually all Audit Committee meetings and is frequently asked to present its perspective on issues. In addition, the Audit Committee meets periodically with the external auditor in private session without management present. Communication between the external auditor and the Audit Committee is ongoing, as frequently as is deemed necessary by either party. IDA's auditors follow the communication requirements with audit committees set out under U.S. generally accepted auditing standards. In keeping with these standards, significant formal communications include:

- Annual financial statement reporting.
- Annual appointment of the external auditors.
- Presentation of the external audit plan.
- Presentation of control recommendations and discussion of the COSO attestation and report.
- Presentation of a statement regarding independence.

In addition to Committee meetings, individual members of the Audit Committee have independent access to the external auditor.

Glossary of Terms

Asset-Backed Securities (ABS): Asset-backed Securities are instruments whose cash flow is based on the cash flows of a pool of underlying assets managed by a trust.

Blend Borrower: IDA Member that is eligible to borrow from IDA on the basis of per capita income and is also eligible to borrow from IBRD on the basis of limited creditworthiness. Given the access to both sources of funds, blend borrowers are expected to limit IDA funding to social sector projects and to use IBRD resources for projects in the 'harder' sectors.

Commitment Authority: Total value of resources available during a particular **replenishment** including donor contributions, internal resources, IBRD transfers, IFC grants and other resources. The Commitment Authority level is monitored periodically to ensure that funding is available to meet commitments and to provide early warning signs of any problems in terms of resource availability.

Completion Point: When conditions specified in the legal notification sent to a country are met and the country's other creditors have confirmed their full participation in the HIPC debt relief initiative. When a country reaches its Completion Point, IDA's commitment to provide the total debt relief for which the country is eligible, becomes irrevocable.

Committee of Sponsoring Organizations of the Treadway Commission (COSO): Committee of Sponsoring Organizations of the Treadway Commission. COSO was formed in 1985 to sponsor the National Commission on Fraudulent Financial Reporting, an independent private-sector initiative which studied the causal factors that can lead to fraudulent financial reporting. In 1992, COSO issued its Internal Control-Integrated Framework, which provided a common definition of internal control and guidance on judging its effectiveness.

Decision Point: Decision by the Executive Directors of IDA to provide debt relief under the HIPC Initiative.

Deputies: Representatives of countries who contribute to the resources of IDA. They include representatives from both **Part I members** and those Part II members who contribute to IDA's replenishments.

Duration: Duration provides an indication of the interest rate sensitivity of a fixed income security to changes in its underlying yield.

Encashment: Draw down (payment in cash) of a promissory note in accordance with a schedule agreed for each replenishment.

Hedging: Hedging is a risk management technique of entering into offsetting commitments to eliminate or minimize the impact of adverse movements in value or cash flow of the underlying instrument or economic condition.

Instrument of Commitment (IoC): A government's commitment to make a subscription or a subscription and contribution to IDA's resources.

Membership votes: Voting rights accorded to IDA members are based on participation in the initial subscription and subsequent replenishments. Membership votes are the same for all members whether they are Part I or Part II.

Net Disbursements: Credit disbursements net of repayments and prepayments.

Part I and Part II Members: IDA's Articles distinguish between two categories of original members -- Part I and Part II -- and provide for a different treatment of the initial subscription payments by each group. Part I members were originally those countries, generally developed countries that contribute to the resources of IDA, whose economic and financial situation justified making the entire amount of their subscriptions available on a freely convertible basis. Part II members are mostly developing countries who subscribe to IDA replenishments for **voting rights**. Some Part II members also contribute to the resources of IDA.

Replenishment: The process of periodic review of the adequacy of IDA resources and authorization of additional subscriptions. Under IDA's Articles, replenishments are required to be approved by IDA's Board of Governors by a two-thirds majority of the total voting power.

Special Drawing Rights (SDR): The SDR is an international reserve asset, created by the International Monetary Fund in 1969 to supplement the existing official reserves of member countries. The SDR is defined as a basket of currencies, consisting of the euro, Japanese yen, pound sterling, and U.S. dollar. The basket composition is reviewed every five years to ensure that it reflects the relative importance of currencies in the world's trading and financial systems.

Subscription votes: Voting rights accorded to IDA members are based on subscriptions. Subscription votes are calculated at a specific cost per vote for each replenishment and are dependent on each member's subscription amount. Additional subscription votes are provided to members who contribute to the replenishment.

Stop Loss: An order to buy or sell a certain quantity of a certain security if a specified price (the stop price) is reached or passed.

Voting Rights: IDA's voting rights consist of a combination of membership votes and subscription votes.