

Review of Internal Controls Over IDA's Operations

World Bank FACT SHEET, April 15, 2009

Background

Established in 1960, the International Development Association (IDA) is the part of the World Bank Group that provides interest-free loans and grants in the world's 68 poorest countries to boost economic growth, reduce inequalities and improve people's living conditions. **The Bank has completed an unprecedented, comprehensive, independent review of internal controls over IDA operations** to fulfill a commitment made to donors during the negotiations of IDA's 14th replenishment (which runs from July 2006 - June 2008).

This review used the rigorous COSO (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 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 3 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). It took almost 3 years to complete.

As IEG noted in its report, the review "has ... broken new ground both in creating methodologies (controls mapping and testing, the Entity-Level Controls Questionnaire (ELCQ), the IEG templates) and in building strong factual knowledge about the Bank's internal controls framework."

Findings and Conclusions

- **All three parties – Bank Management, IAD and IEG -- reached a similar conclusion regarding the overall adequacy of the internal controls over IDA's operations, subject to issues identified in specific areas. As is normal for such exercises, the review identified a number of deficiencies and areas that require strengthening, ranging from minor, to significant, to a "material weakness."**

As IEG has stated, "**with some important qualifications, IDA's internal controls framework operates to a high standard overall, giving reasonable assurance that the controls operate effectively.**"

- IEG found "**evidence presented by management...gives reasonable assurance—except for weaknesses identified in certain parts of the overall framework—that controls operate effectively...** [and subject to identified exceptions] provide Senior Management and the Board with reasonable assurance that the **three COSO objectives are being achieved: (i) reliable financial reporting, (ii) compliance with policies and procedures, and (iii) the efficiency and effectiveness of operations.** Evidence of controls effectiveness at the entity level (based on questionnaire results) includes pass rates ranging from 92 percent to 95 percent, depending on the method. The earlier evidence at the transactions level includes a pass rate of 93 percent (document-based testing of key controls)."

Management takes the issues identified by the review very seriously and has formulated and begun implementation of a robust plan of actions to address them. IEG called management's assessment "transparent, well documented, comprehensive" and noted that management's remedies "correspond well" to IEG's recommendations. IAD and IEG have endorsed Management's actions as appropriate to remedy the issues identified.

- **Management, IAD and IEG also agreed on the nature of the deficiencies uncovered in the areas of: (i) investment lending, (ii) risk management, (iii) integration of fraud and corruption prevention into operations, (iv) financial management and procurement, and (v) information technology (IT) and processes and systems for Analytic and Advisory Activities (AAA).**

Though both IEG, and IAD found that the overall framework is robust, they identified weaknesses concentrated in a few key areas, with some differences as to the degree of the deficiencies.

- IEG found **six significant deficiencies overall and a material weakness in “risk of [not actual incidence of] fraud and corruption [F&C].”** IAD found no material weaknesses but significant deficiencies in fiduciary, entity-level, information technology, and fraud and corruption controls.
 - IEG said that **one finding of a “material weakness” should be considered “quite respectable”** for this type of first of its kind, very detailed exercise for IDA.
 - Using COSO standards, **IEG rated IDA Controls overall as “satisfactory with qualifications.”**
 - **IEG noted that similar reviews of the US Treasury and USAID utilizing the same COSO methodology identified 8 material weaknesses in Treasury (2004) and 4 in USAID (2007).**
- In setting out its findings, **IEG has noted:**
 1. The **Bank’s progress in building its governance and anti-fraud and corruption agenda**, including specific **tools recently put in place to address F&C** issues at the project and country levels. IEG stated however that it is too early to assess effectiveness of these measures;
 2. **The challenges of fraud and corruption for all development partners;**
 3. A **high level of effectiveness of IDA’s internal controls compared to results in other organizations of similar size and complexity** (with a “finding of single material weakness (together with some significant deficiencies) **should overall be considered a quite respectable outcome** from the first (and very detailed) exercise of its kind for IDA.”
 4. **The importance of this first of its kind review among IFIs**, and its impact on accelerating management actions in strengthening IDA’s controls, especially in the Governance and Anti-Corruption area.

This exercise is a snapshot in time dating back about 12 months. Much has been done already to strengthen controls in the fraud and corruption area, particularly in response to the Volcker report and the India Detailed Implementation Review (DIR).

Management considers the issue of F&C to be a top priority, with the highest of standards to be reached as soon as possible. It is important to recognize that F&C refers to risk of F&C in WBG supported projects, not F&C by WBG staff.

Going Forward

Bank management takes these issues extremely seriously and has formulated a robust plan to address the results of the IDA Controls Review:

- **Improve efficiency, effectiveness and controls for Investment Lending** by focusing resources on higher risk projects; strengthening oversight of project implementation and consolidating multiple rules into clear principles to inform design and processing.
- **Strengthen risk management capacity, incentives and accountability at the project and institutional levels.**
- **Better integrate fraud and corruption prevention into operations.**
- **Tighten fiduciary controls.**
- **Strengthen role of Information Technology (IT) in risk management and improve processes and systems for AAA.**

Many of these actions are in process or will be completed by June 2009, building on ongoing efforts.

To ensure effective monitoring of, and transparency and accountability for implementation of these actions, management is establishing an oversight body -- a special Implementation Oversight Panel (IOP) -- to monitor and periodically report to the President and the Audit Committee on the implementation progress. The IOP will be co-chaired by an outside party and the Bank’s Chief Financial Officer and Vice President for Operations and Country Services, with IAD, IEG and INT participating as observers.