The Safeguards Policy:

Independent Panel's Advisory Report to the Executive Board of the IMF

July 1, 2010

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The panel wishes to acknowledge the assistance and cooperation extended to it by the staff of the Fund, the staff of the World Bank, and the central banks of The Gambia, Ghana, Latvia, and Pakistan. The panel also wants to acknowledge the secretariat assistance provided by Marylyn G. King of the Fund staff in coordinating our work and helping in our preparation of the report.

EXECUTIVE SUMMARY

This report by the external panel of experts ("the panel") examines the effectiveness and appropriateness of the safeguards policy over the ten years since the inception of the policy, and most particularly in the five years since its last review. Furthermore, the panel, drawing on its research and experience, aims to establish a course for the Executive Board to consider that would help the safeguards policy continually improve, adapt to changing world conditions, and remain viable and relevant for the next decade. In gathering data to form its opinion, the panel (i) consulted with stakeholders in the policy (including central bank authorities, IMF Executive Directors' offices, Fund and World Bank staff, and international audit firms), (ii) examined safeguards and other Fund-specific documents, and (iii) researched international reference materials.

The panel finds the existing framework for the safeguards policy has been effective overall in achieving its objective to mitigate potential risks of misuse of Fund resources and misreporting of monetary program data. Of the 165 assessments conducted since 2001, only six cases of misreporting and three cases of governance abuse have occurred, resulting from deliberate overrides at the highest levels. In these cases, safeguards measures have been instrumental in either detection or correction of the problems. Stakeholders in the policy also voiced to the panel their approval and support of the policy. The staff that conducts the safeguards assessments and monitoring activities implements the policy with competence and has adapted it to developments in central banks. A beneficial by-product of the policy has been the progress in central banks toward adopting international standards and best practices, thereby making central banks stronger agents for IMF member countries and helping them improve the international monetary system.

Against the backdrop of the global economic crisis that began in late 2008, the safeguards policy is under more stress to succeed now than ever before. IMF member countries are seeking unprecedented levels of financial resources from the Fund, with SDR 51,920 million outstanding as of 31 May 2010. IMF lending is also experiencing a shift in the proportion of those resources for budgetary support, with nearly 30 percent of the value of the current Stand-by Arrangements (SBAs) as of May 2010 being allocated for budgetary support, totaling SDR 17,554 million.[1] It is paramount to the Fund that these resources and its reputation as a prudent lender be safeguarded in this high-stakes economic climate.

[1] SDRs are Special Drawing Rights, the unit of account at the IMF. Data on outstanding credit to the Fund are drawn from the IMF external website. Data on budgetary support were provided to the panel by staff economists.

Critical analyses of the causes of the crisis have resulted in forceful calls from authorities and other professionals around the globe for improved corporate governance, strengthened risk management, greater compliance with international standards, and increased transparency. The panel recommends that the safeguards framework be gradually enhanced, through a continuous improvement process, to address these pressing concerns in a sharply focused and explicit way. This report provides details in each of these areas.

The panel endorses an expansion of the safeguards policy, which currently covers only central banks, to include safeguards assessments that target state treasuries when Fund resources are provided for budgetary support. Existing data from other IMF and World Bank assessments may be leveraged to create a safeguards report of a state treasury, provided an independent safeguards team conduct due diligence in ascertaining the quality of the data. The cornerstone of such assessments, like those for central banks, is the independent perspective of the staff conducting the assessment. In this context, staff conducting the assessment should not be assessing its own work or have a vested interest in any specific implementation plan.

Finally, the panel urges staff to continue its efforts to improve communication with central bank authorities and Fund staff in other departments. The objectives of the policy are best served when all stakeholders fully understand the issues and are engaged in the process.

I. INTRODUCTION AND BACKGROUND

1. **The objective of the safeguards policy is to mitigate potential risks of misuse of Fund resources and misreporting of monetary program data.** This objective contributes to the larger goal of safeguarding Fund resources themselves, a goal most strongly addressed in the economic programs for member countries using Fund resources. Program design and effectiveness require competent central bank management of and accurate reporting on monetary resources, including Fund disbursements. Central banks, as agents responsible for managing members' international reserves and Fund resources, are crucial to program success. For this reason, the safeguards policy reviews the central banks' integrity of operations, identifies risks, and recommends and follows through on corrective actions where needed. The safeguards policy relies on others who perform oversight or testing of some of the key information, such as the independent and internal auditors, and an independent audit committee. The safeguards methodology, applying a framework known by the acronym ELRIC, examines five essential elements of central bank operations: (i) external audit, (ii) legal structure and independence, (iii) financial reporting, (iv) internal audit, and (v) internal controls.[2]

2. Now, ten years after the inception of the safeguards policy, an external panel of experts ("the panel") has been assembled to advise the Executive Board in its third review of the policy. The panel comprises Mr. Lynn E. Turner (Chair), current Senior Advisor to an international forensics and economic consulting firm, former Chief Accountant of the Securities and Exchange Commission, and member of the 2000 expert panel for the IMF safeguards policy; Dr. Ranee Jayamaha, current Advisor to His Excellency the President of Sri Lanka and former Deputy Governor of the Central Bank of Sri Lanka, and Dr. Len Konar, current Director and former Chair of the Audit Committee of the South African Reserve Bank and former Chair of the External Audit Committee of the IMF.[3]

3. **The work of the panel was defined as follows:**[4]

- Advising the Executive Board on the continued appropriateness of the ELRIC framework, taking into account the adaptations made by staff in applying the framework over the last decade and the evolution in governance and control practices in the public and private sectors since the introduction of the policy. Since safeguards reports are not circulated to the Executive Board, it is expected that the panel's

[2] The staff paper concurrently being presented to the Executive Board summarizes the history of the policy, the process of conducting safeguards assessments and monitoring, and the resulting documentation.

[3] Curricula vitae of the panel members are provided alphabetically in Attachment I.

[4] This work was defined in the Issues Note provided to the panel and the Executive Board.

review of the adequacy and coverage of safeguards reports would be a key input for its work in assisting the Executive Board with the policy review.

- Assessing the operation of the risk-based monitoring framework and its effectiveness during respectively: (i) the period of an arrangement and (ii) thereafter for as long as Fund credit is outstanding.

- Sharing their views on other aspects being considered under the policy review, in particular: (i) how to handle safeguards issues in the context of arrangements that involve direct budgetary support; and (ii) changes that might be considered for the dissemination of safeguards findings.

4. **The panel's method of inquiry involved the following activities:** (i) researching safeguards assessment reports of central banks and other safeguards materials, (ii) researching applicable literature from other international and professional organizations, (iii) consulting selected central banks and drawing on their own central banking experience, (iv) discussing Fund-specific topics for external auditing with KPMG (v) consulting offices of Fund executive directors (EDs), and (vi) consulting key staff at the Fund and the World Bank.[5]

II. EFFECTIVENESS OF THE CURRENT FRAMEWORK

5. **During the ten-years the safeguards policy has been in effect, the Fund has committed SDR 224,674 million through 185 new and augmented arrangements; as of 31 May 2010, SDR 51,920 million remain outstanding**[6] The high volume of safeguards assessments and subsequent monitoring required for these arrangements have been substantive in nature. They have effectively met the objectives of the policy by providing reasonable, but not absolute, assurance of sound central bank operational frameworks and standard reporting mechanisms, thus strengthening the programs in place for Fund arrangements. For example, in response to safeguards recommendations, 43 central banks have, for the first time, reconciled key program data with accounting records.[7]

6. **The data suggest that safeguards monitoring practices have effectively deterred or detected misreporting cases.** The vast majority of central banks are properly reporting

[5] A list of documents reviewed and attendees at these meetings are provided in Attachment II. Summaries of the topics discussed are provided in Attachment III.

[6] Attachment IV contains a table of annual amounts of arrangements, taken from the Fund Annual Report 2009 and the Quarterly Financial Statement of January31, 2010. The credit outstanding is taken from the IMF external website at <http://www.imf.org/external/np/fin/tad/extcred1.aspx> on 24 June 2010.

[7] *Safeguards Assessments-2009 Update*, Table 5 (staff paper).

and managing Fund resources now that safeguards measures are in place. Although there are no data to compare results before and after the safeguards policy was implemented, the data analyzed since the safeguards policy suggest that a misuse or misreporting event such as those that triggered the policy is not as likely to occur now or go undetected. Of the 165 assessments conducted, misreporting has been identified in only six cases (three of which are since the 2005 policy review), and governance abuse in three cases.[8]

7. **The safeguards monitoring framework introduced in 2006 has also proven broadly effective and efficient**. Following the 2005 review, a risk-based framework was introduced for monitoring safeguards developments in central banks once an assessment has been completed. Under this framework, staff establishes a monitoring intensity level based on a prescribed set of risk factors that include elements of ELRIC as well as other considerations: the level of exposure to the Fund, the country's corruption index, past history with Fund arrangements, status of safeguards recommendations, audit quality, governance, and legal changes. The framework is effective in that it has enabled staff to monitor the implementation of key safeguards measures as well as identify instances where safeguards measures have not been sustained, such as when an external audit has ceased to be performed in accordance with international standards. Efficiency has been achieved through the ready availability of monitoring information in preparing for an update assessment, and a reduced need for staff monitoring visits to central banks to verify information and safeguards developments. Despite increasing difficulties in obtaining monitoring information, such as audit reports and management letters, as time passes subsequent to the conclusion of a Fund arrangement, the panel believes it is important to continue monitoring the borrower as long as Fund credit remains outstanding. The panel believes that a central bank's failure to provide monitoring information should be noted in country staff reports. The panel also believes the level of monitoring subsequent to the end of disbursements being made and prior to their repayment should reflect the level of risk identified by the safeguards program, with greater scrutiny provided to higher risk borrowers.[9]

8. **In consulting with central banks, ED offices, and Fund staff, the panel found broad approval for the safeguards policy and its ELRIC framework; these constituencies reported to the panel that they believe the policy to be effective overall and useful in achieving the stated objectives of the program, helping central banks adopt best practices, and protecting the reputation of the Fund.** In the expert opinion of the panel, the ELRIC framework adequately identifies weaknesses in processes and controls

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[8] These figures are as of end March 2010, excluding the 27 transitional assessments done in 2000. The staff paper details the circumstances of the misreporting and governance abuse cases, the safeguards involvement in detection and correction, and a discussion of lessons learned from these cases.

[9] See Attachment V for additional details on the risk-based monitoring framework.

currently being examined at central banks that could lead to misreporting and misuse. The panel sees evidence, too, in safeguards monitoring results and annual update reports of the specific governance improvements that central banks cited: the establishment of audit committees, adoption in whole or in part of international financial and accounting standards, enhanced independence, and better internal controls and auditing processes.[10] And finally, given the safeguards policy originated from fraud cases that exposed the Fund's insufficient oversight at central banks, the panel strongly agrees with staff and ED offices that having a robust safeguards policy is imperative for the Fund's reputation.

9. **The panel believes the safeguards staff is well qualified to adapt the ELRIC framework as needed to address emerging concerns in the global economy.** The caliber of the safeguards staff is exceptional. The panel has met with and had discussions with the safeguards staff, and has examined some of its monitoring procedures and work. Based on this evidence and the excellent feedback received from central banks consulted, the panel finds the staff's skill set, experience, judgment, and professionalism to be of high quality, and commends staff in making the safeguards policy succeed in its objectives and gain the respect of member countries.

III. Recommendations for Continuous Improvement

10. In the ten years since the inception of the safeguards policy, much has changed in the global economic landscape and the Fund's role in global policies. In the context of a series of economic crises and now looming sovereign liquidity problems, the Fund is being called upon to respond with resources of unprecedented amounts, and with unprecedented public scrutiny. Providing reasonable assurance that these resources are being managed responsibly and transparently by recipient member countries is integral to the Fund's reputation and, therefore, its ability to carry out its mission.

11. For the safeguards policy to adapt to changing global and financial conditions, the panel believes the Fund should consider implementing the recommendations proposed below. These recommendations would involve continuous improvements to the ELRIC framework over time; they would involve gradual work toward meeting new or heightened expectations.

A. Governance

12. **Developments in financial markets and among financial institutions during the past decade have highlighted the need for good governance—principles enshrined in a framework that sets an ethical tone at the top of the organization and governs the entire organization.** In its *Principles of Corporate Governance,* the Organization for

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[10] *Safeguards Assessments-2009 Update*, Table 5 (staff paper).

Economic Co-operation and Development (OECD) specify "The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders."[11] Without a sound governance framework, other systems, controls, and procedures fail:

> [In the financial crisis,] risk management systems have failed in many cases due to corporate governance procedures rather than the inadequacy of computer models alone: information about exposures in a number of cases did not reach the board and even senior levels of management, while risk management was often activity rather than enterprise-based. These are board responsibilities. In other cases, boards had approved strategy but then did not establish suitable metrics to monitor its implementation. Company disclosures about foreseeable risk factors and about the systems in place for monitoring and managing risk have also left a lot to be desired even though this is a key element of the Principles. Accounting standards and regulatory requirements have also proved insufficient in some areas leading the relevant standard setters to undertake a review. Last but not least, remuneration systems have in a number of cases not been closely related to the strategy and risk appetite of the company and its longer term interests.[12]

Similarly, the Group of 30 calls for greater emphasis on governance: "Institutional policies and standards must be strengthened, with particular emphasis on standards for governance, risk management, capital, and liquidity."[13]

13. **For the safeguards policy to adapt to the changed financial global climate and respond to these calls to action from prominent organizations, the panel believes that the ELRIC framework needs to sharpen its focus on governance.** Some measures of good governance, such as legal structure and independence and the existence of independent audit committees, are already key components of ELRIC. However, these measures alone have proven to fall short in ensuring good governance. The OECD asserts "the financial crisis can be to an important extent attributed to failures and weaknesses in corporate governance arrangements. When they were put to a test, corporate governance routines did not serve their purpose to safeguard against excessive risk taking."[14]

14. **The panel, drawing on its own experience and research, believes it is important that staff, when assessing the integrity of a central bank's operations, explicitly evaluate the bank's approach to corporate governance based on the following**

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[11] "Responsibilities of the Board." *OECD Principles of Corporate Governance.* OECD, 2004.

[12] Kirkpatrick, Grant. "Main Conclusions." *The Corporate Governance Lessons from the Financial Crisis*. OECD Steering Group on Corporate Governance, 2009.

[13] "Core Recommendation III." *Financial Reform: A Framework for Financial Stability.* Group of 30, 2009.

[14] Kirkpatrick.

principles: independence, responsibility, accountability, fairness, transparency, discipline, and social responsibility.[15] Good corporate governance is essentially about effective, responsible leadership. The central bank's board needs to commit to high standards of governance as its ethical approach to business. The central bank needs to be seen as conducting its business with integrity, building from a foundation of compliance with relevant local laws and regulations, and international standards. The central bank should engage in continuous improvement of its governance system by periodically reviewing its code of conduct and ensuring its values are spread to all employees. Adherence to high standards of corporate governance forms an essential underpinning to the central bank's ability to deliver on its core objectives.

B. Risk Management

15. In the wake of the global economic crisis, experts agree that all financial institutions around the globe must improve their management of risk. To quote the G20, "Major failures of regulation and supervision, plus reckless and irresponsible risk taking by banks and other financial institutions, created dangerous financial fragilities that contributed significantly to the current crisis. A return to the excessive risk taking prevalent in some countries before the crisis is not an option."[16] The Basel Committee on Banking Supervision declares "A key characteristic of the financial crisis was the inaccurate and ineffective management of liquidity risk." [17]

16. It is beyond dispute that financial and business risks are proliferating: continuity, sustainability, stability, and reputation are threatened. At the same time, the corporate scandals of the past decade have intensified focus on the role and responsibility of governing boards and their members. Risk is now considered a board-level responsibility at central banks.[18] The panel believes, based on its interviews, that the boards of central banks now understand the need to consider risks more seriously and deal with them in a more thoughtful manner than they have in the past. While risk management may be centralized

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[15] Adapted from CLSA Emerging Markets and from the King Code and Report on Corporate Governance for South Africa. See Attachment VI for definitions of these principles.

[16] "Strengthening the International Financial Regulatory System." *Pittsburg Summit*. Group of 20, September 2009.

[17] "International framework for liquidity risk measurement, standards and monitoring." Basel Committee, December 2009.

[18] *Financial Reform,* Group of 30, p. 19 states "The need for high standards of institutional governance and risk management must be recognized, with emphasis on: Engaged and knowledgeable independent boards of directors focused on long-run performance." In the panel's discussion with the central banks of The Gambia, Ghana, and Latvia, these authorities agreed that risk management is a board-level responsibility.

and overseen by the board, it is also important to the safeguarding of a central bank's (and the Fund's) resources that a risk management culture be embedded at a bank-wide level.

17. **Central banks should be the first institution to move away from a silo approach to risk mitigation and establish an integrated risk management framework (IRMF) because they are in the business of monitoring and providing economic stability.** The Basel Committee notes that "Throughout the global financial crisis, …unprecedented levels of liquidity support were required from central banks in order to sustain the financial system…"[19] Central banks need an IRMF to best position them to serve as a sustaining and stabilizing force, a function that is compounded by the many competing business needs for which it must manage risk. For example, central banks must balance achieving external sector stability with maintaining international reserves. They must also consider the risks of borrowing and creating money to meet budget deficits (monetization). And in several advanced economies, central banks have had to weigh the effects of bailing out large institutions against the risk of creating high-powered money and increasing liquidity and inflationary pressures. An IRMF would provide the necessary mechanisms, processes, and procedures to help central banks take prompt action, fill gaps, and enhance accountability and transparency. How central banks manage risk, the resulting success rate of that effort, and which processes and mechanisms they use should be made known to the public with an adequate level of transparency. The effectiveness of the framework may differ with the magnitude of risks and the level of sophistication in the central bank, but the existence of an IRMF is absolutely essential for central banking.

18. **Just as staff engages in risk management on behalf of the Fund by conducting safeguards assessments and monitoring of central banks, the panel believes staff should extend that risk management to include an explicit assessment of how well central banks manage their own risks.** The effectiveness of central banks in managing their own risks ultimately affects the degree of risk exposure for the Fund. The panel believes a well-established IRMF creates a healthier, more reliable central bank. An IRMF helps identify, detect, and mitigate those risk events or characteristics that so often contribute to and result in misuse, misreporting, or even fraud regarding Fund resources, as well as resources of other international organizations providing assistance to the central bank.

19. **The current ELRIC framework does not adequately consider how management and governance of the central bank assess risks arising from activities of the bank, financial markets, banking industry, and global economy.** These activities carry risks that can affect strategy, finance, stability, sustainability, and other issues. The central bank needs to foster a risk-aware corporate culture in all decision making and to commit to managing all risks in a proactive and effective manner. To support this commitment, risk

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[19] Basel Committee.

must be analyzed and must inform management decisions at all levels in the central bank. Risk factors for a central bank as a whole require the attention of the board of governors and the appropriate levels of management, including a Chief Risk Officer (CRO) or risk management committee (RMC) or equivalent. A safeguards assessment should determine whether the CRO/RMC operates with clear and independent lines of reporting to the board, and that it focuses on high priority items: critical success factors and risk performance indicators in the context of the bank's established mission, strategic goals, and operational objectives.[20]

20. **The safeguards assessment methodology should consider whether a central bank establishes a benchmark and framework for assessing risk, and whether the risk management system operates effectively.** The panel heard during its interviews with central banks that any risk management assessment will need to be based on a reasonable framework or benchmark, and the panel agrees. Risk management could follow international guidelines, such as ISO 31000, which "provides principles and generic guidelines on risk management,… can be applied throughout the life of an organization, and to a wide range of activities,… [and is intended to] be utilized to harmonize risk management processes in existing and future standards."[21] Risk management could use a framework such as that developed by the Committee of European Banking Supervisors (CEBS) or the Committee of Sponsoring Organizations (COSO). CEBS has established a set of high-level principles for risk management that include: (i) governance and risk culture, (ii) risk appetite and risk tolerance, (iii) the role of the Chief Risk Officer and risk management function, and (iv) risk models and integration of risk management areas and a new product approval policy and process.[22] COSO identifies the components of risk management as: (i) internal environment, (ii) objective setting, (iii) event identification, (iv) risk assessment, (v) risk response, (vi) control activities, (vii) information and communication, and (viii) monitoring. The safeguards assessment would judge the effectiveness of risk management based on whether all components of risk management are present and functioning effectively.[23]

C. Transparency in the Safeguards Program

21. **The panel believes that, with the established credibility of the safeguards program, it is time to begin a gradual move toward increased transparency in the**

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[20] "High Levels of Risk Management," Committee of European Banking Supervisors, 2010, provides guidelines for establishing a risk management function.

[21] "Abstract." *ISO 31000: 2009*. International Organization for Standardization, 2009.

[22] *High Level Principles of Risk Management.*CEBS, 2010.

[23] *Enterprise Risk Management – Integrated Framework*. COSO, 2004.

safeguards program over the next decade. Confidentiality in safeguards reports during the first decade of the policy has served the Fund and its members well. Confidentiality has helped to build members' trust in the policy and has provided the context for staff to develop detailed, objective, and candid safeguards reports. However, transparency in governments and the public sector has proven useful and beneficial. Transparency is expected more now than it was ten years ago, and the justification for it is solid: to encourage good governance and accountability in central banks, a goal that is in line with the mission of Transparency International, which is "to create change towards a world free of corruption."[24]

22. **The panel is aware that obtaining support for transparency will prove to be a challenge.** Some central banks are not ready for it, and some staff members believe it will strain relations between the Fund and its member countries. However, there is precedence for greater transparency in other Fund and World Bank papers: country reports, portions of reports created under the Financial Sector Assessment Program (FSAP), Reports on the Observance of Standards and Codes (ROSC), and Public Expenditure and Financial Accountability (PEFA) reports are currently published. The safeguards policy should work toward a similar level of publication of safeguards information. The panel understands that transparency tends to be an evolutionary process and recognizes that initially some safeguards information may be made transparent in a summary form in a manner consistent with the goals of the IMF Code of Good Practices on Fiscal Transparency and the IMF Code of Good Practices on Transparency in Monetary and Financial Policies. Then, over time, greater amounts of information in greater detail can be made transparent.

23. **To accomplish what is expected to be a reasoned and gradual move toward transparency, specific recommendations include:**

- That as a first step, the safeguards assessment report format include a bulleted list at the beginning that identifies the top few safeguards-related risk factors for lending, and that the bulleted list be published in the country staff report. During safeguards monitoring, any updates to the list of risk factors would similarly be published in the program review staff reports. Such information would better inform the Executive Board when making lending decisions, and would better inform the public, as country reports are circulated to the Board and are typically published.

- That periodically, but no less than every other year, the Fund publish safeguards findings in aggregate, anonymous form that reveal issues, not central banks, and indicate corrective actions taken. Such information could serve as an educational tool for all central banks (and other interested parties, such as external auditors and donors). It would complement the safeguards seminars as a forum for the exchange of

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[24] "What Is Transparency International?" <http://www.transparency.org/about_us> 22 June 2010.

lessons learned and promote the understanding of the safeguards policy and its value to a broader audience. The aggregate reports should indicate the effectiveness of governance practices and risk mitigation methods in exemplary countries.

- That central banks be encouraged to voluntarily publish their own safeguards action plans and accomplishments. This practice would help them strengthen credibility with their constituency and could foster a "race to the top" by banks. By contrast, maintaining confidentiality enables the poorest performers implicitly to set the standard.

D. Transparency in Financial Reporting

24. **The panel endorses full compliance with both International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA), which the ELRIC framework urges for central banks to adopt.** Central banks that have undergone safeguards assessments are moving toward these standards; some have fully complied with IFRS while others have, unfortunately, complied only partially. The resulting improvements have benefitted the Fund by enabling improved transparency and accountability of central banks in properly managing and reporting on Fund resources. Consequently, lending members have a reasonable assurance that their resources have sufficient Fund oversight, and borrowing members gain credibility with the public. The Fund's reputation as a prudent lender is strengthened in the process.

E. Fraud Detection

25. **An effective governance framework should include consideration of the central bank's whistle-blower policy.** One of the key components of ELRIC is verification of accurate financial reports. The audit committee, external audit, and internal audit are all important functions that help achieve this objective. The panel strongly supports the continuation of these functions as part of the safeguards framework. However, research by the Association of Certified Fraud Examiners has shown that misreporting is most commonly detected through the establishment of an independent whistle-blower program: "Occupational frauds are much more likely to be detected by tip than by any other means. This finding has been consistent since 2002 when we began tracking data on fraud detection methods."[25] Transparency International reports "The value and importance of whistleblowing in the fight against corruption is becoming increasingly recognised. International conventions commit signatory countries to implementing appropriate

[25] *Report to the Nations on Occupational Fraud and Abuse*, p. 4. Association of Certified Fraud Examiners, 2010.

legislation, and several countries have proposed legislation under consideration."[26] Accordingly, the panel believes that as part of its assessment of internal controls, staff should consider recommending a whistle-blower program if one does not exist, and an assessment of it if one does exist: its independence, and resolution of issues through the roles of the internal auditors, audit committee, and independent auditor. This could be accomplished by the Fund staff directly or by requesting a report on the program by the audit committee, internal auditor, or external auditor.

26. **The panel understands that in some countries such a program may not exist due to cultural considerations.** Cultural practices may take a long time to change, but through enhancement of awareness and illustration of success stories, the time period can be shortened. The Fund should bear in mind that in the past, not all central banks have had the requisite levels of independence or the audit committees the safeguards policy expects; but over time, countries are complying with those expectations and are better off for doing so. A whistle-blowing policy would be a similar situation. The panel urges staff to work with the officials of central banks to consider methods of implementation or alternative structures that would achieve the same results.

F. External Audit

27. **The staff's reliance on external auditors poses a vulnerability in the policy framework when the audit quality does not provide the high level of assurance required by international standards.** Events in the news provide cause for the Fund to be skeptical of the big four audit firms.[27] Central banks and staff also noted the quality of external auditors varies around the globe; some auditors do not have adequate expertise in central bank and Fund-specific issues such as reporting of net international reserves. Poor quality audits, where they occur, weaken the level of assurance a safeguards assessment can provide and continue to draw on the staff's level of effort during a safeguards monitoring cycle.

28. **The panel suggests that staff, when applying the ELRIC framework, go beyond identifying the external auditors' processes and also attempt to assess the quality of their work by examining auditors' peer review reports or regulators' reports.** Furthermore, staff may want to examine reports on the quality of audits in a particular country, if available from a peer review process or regulators. Consideration should also be

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[26] "Towards Greater Protection of Whistleblowers." Transparency International. <http://www.transparency.org/global_priorities/other_thematic_issues/towards_greater_protection_of_whistleblowers> 22 June 2010.

[27] Incidents of fraud involving Price Waterhouse Coopers in Japan and India, and Ernst & Young in Hong Kong are some examples.

given to the oversight structure for auditing firms in the respective country and how that may impact audit quality.

29. **The panel recommends the Fund attempt annual meetings with senior partners of the international institutions of the big four auditing firms to discuss areas of concern, significant risks, and suggested improvements.** Topics for discussion may include the firm's compliance with International Standards on Auditing (ISA), standards on quality controls, and understanding and knowledge of high risk audit areas such as reserves. The panel has tested this proposal with a senior KPMG partner and learned that KPMG is very willing to have discussions with the Fund on these topics; the panel encourages staff to reach out to the remaining firms (PricewaterhouseCoopers, Deloitte, and Ernst & Young) similarly. The Fund may also look into the feasibility of developing and providing educational materials aimed at external auditors, covering Fund-specific areas of competency such as international reserves.

G. External and Internal Communication

30. **The data show that communication with central banks beyond the on-site mission for a safeguards assessment is successful in achieving its goals**: central banks implement committed safeguards recommendations at a 90 – 95 percent rate over the last three years, and at a 70 – 79 percent rate for other recommendations.[28] Staff also delivers semi-annual safeguards seminars, which central banks informed the panel they rate highly, consistent with seminar evaluation results. Safeguards fact sheets and annual reports are posted on the external website. These results indicate that staff has taken action on the 2005 external panel's suggestions for improving external communication. Nevertheless, some of the central banks consulted expressed an interest in more frequent and personal contact with staff, such as via tele- or videoconferences rather than such heavy reliance on e-mails, to maintain the one-to-one relationship established during mission and to enhance the on-going dialog. This response is consistent with the findings of the 2005 panel.[29] The panel believes the quality of the relationship between the Fund and central banks could benefit from these adjustments in communication. However, the panel disagrees with the suggestion of one bank that the safeguards process should merely be a collaborative process between Fund staff and the bank. The panel notes that other banks urged staff to go in the other direction and actually perform testing during an assessment to substantiate the findings that are based on interviews. The panel cautions the Fund to be aware that central banks seem interested in

[28] *Safeguards Assessment—2009 Update,* Annex IV (staff paper).

[29] This recommendation reiterates the 2005 external panel's report, which stated "Central banks and panel members observed the need for better and more frequent communication between the IMF and central banks on safeguards issues. To address this issue, the panel recommends that the IMF enhance its communication with key safeguards stakeholders by employing a variety of channels including workshops and the establishment of a website."

technical assistance following an assessment, which is beyond the mandate of the safeguards policy.

31. **A set of self-assessment templates based on the safeguards framework should be developed.** By providing this material to all member countries, the Fund would be encouraging the authorities to take ownership of and responsibility for the effective operation of the components of ELRIC. The Fund could effectively expand the capacity of safeguards assessments without additional on-going demand for staff resources. With such templates, central banks could proactively conduct their own initial safeguards assessments and may be better positioned to implement structural, control, and operational improvements. Central banks could also conduct their own update assessments during the safeguards monitoring phase. Results from the self-assessments, particularly if made transparent, would facilitate lending if an arrangement is requested in the future, easing the work of safeguards staff and potentially reducing safeguards reforms needed in program design.

32. **The panel backs the current offering of voluntary safeguards assessments conducted by staff to any member country when no arrangement with the Fund is involved.** It is advisable, if feasible, for a country to undergo a staff assessment at a time when it is not under the strain of seeking a Fund arrangement. At such a time a country would have more capacity—financially, operationally, and in terms of management attention—to implement safeguards recommendations efficiently and effectively. Preemptive assessments would bring more central banks in line with best practices, and therefore could facilitate Fund arrangements and program design and reviews in the future.

33. **It is important to continue raising awareness within the Fund in order to advance the objective of the safeguards policy.** In speaking with area department representatives, the panel learned that some of them are only minimally aware of the relevance between safeguards activities and their own work in program design and reviews.

H. Information Technology

34. **Ideally, central banks would have seamless electronic mapping of data from their own accounting systems to data reports provided to the Fund.** Many central banks do not currently have automated systems for accounting and data reporting. Processes where there is a lack of technology, requiring largely manual data entry into spreadsheets or mapping of data from one report format to another, are inherently risky for either inadvertent or deliberate misreporting. As central banks become more technologically sophisticated over the next decade, safeguards assessments should consider the effectiveness of any new systems implemented and the ability of central bank staff to use the systems properly.

35. **Information technology is an important component of an integrated risk management framework.** Risks can best be identified and mitigated if end-to-end transactions can be examined. Especially the general ledger, which contains all domestic and international transactions of a central bank, should be automated. If not, identifying and mitigating risks amid decentralized accounting systems and financial reporting systems may be unattainable.

IV. Safeguards in the Context of Budgetary Support

36. **In the last few years, the Fund has experienced a shift in the nature of lending, toward more budgetary support than in the past, and with that shift comes an associated shift in the nature of the risk to Fund resources.** Based on data from the countries with SBAs as of May 2010, resources for budgetary support accounted for an average of nearly 30 percent (including 100 percent for Iraq and Latvia), and totaled SDR 17,554 million.[30] Given this magnitude of risk, the success of the safeguards policy to date may become diluted if no counterpart to the central bank safeguards framework is applied to state treasuries receiving this proportion of Fund resources. In addition, the Fund exposes itself to reputational risks if it provides budgetary support without a targeted safeguards program or with a safeguards program that is insufficient. Such an approach raises the question of why the Fund has a safeguards program for lending directly to central banks but not for lending for budgetary support. The panel believes that the Fund should take steps toward developing a credible mechanism for safeguarding resources used for budgetary support; otherwise, any assurances of safeguards at the central banks is only partial and potentially misleading about the overall risk to Fund resources.

37. **The panel recommends that staff carefully circumscribe an approach that will move the Fund in the direction toward safeguarding Fund resources at the treasury level, where the greatest budgetary-related risk lies.** Emphases must be placed on keeping any new approach aligned with the original safeguards policy objective and the Fund's mandate. The objective of the approach would be to provide a reasonable, but not absolute, level of assurance that there is not misuse of Fund resources and misreporting of data. This includes ensuring expenditures are properly authorized, that reporting of financial information and data is accurate and timely, and that internal and independent audits are done properly.

38. **The panel finds merit in a framework proposed by staff for safeguards assessments of state treasuries**. This framework should be consistent with, and incorporate the fundamental principles of, the Code of Good Practices on Fiscal Transparency adopted

[30] The data reflect the total budgetary support expected by the time the arrangements are concluded. Data were provided by economists in area departments and the Strategy, Policy, and Review (SPR) department.

by the Fund in 1998. The proposed framework addresses seven criteria, which the panel endorses with the following further elaboration:[31]

- A single state treasury account should be established in the central bank through which all government transactions are processed.

- Proper authorization of budgetary expenditures. Clear procedures should be established for timely budget execution, monitoring, and reporting. This includes proper authorization of budgetary expenditures and comparisons of actual expenditures with approved budgets in a manner that provides accountability to the public.

- Regular reconciliation of all government expenditure accounts in the state treasury should occur in a timely manner.

- Proper accounting, according to international standards, of all government transactions in the state treasury. Timely, accurate, and transparent accounting and financial reporting should be done according to applicable international standards, of all government transactions. The accounting information systems, including internal accounting controls, should provide a reliable basis for tracking finances with necessary supplemental detail for revenues and expenses. The financial information should be presented in a way that facilitates policy analysis and promotes accountability.

- Independent audit, according to international standards, of final accounts. Both an independent audit of final accounts in accordance with international standards, as well as an independent and transparent internal audit function should be established. Public finances should be externally scrutinized by an independent national body.

- Observations of auditors to improve financial management processes taken on board systematically. A process should be implemented for the improvement of financial management processes and internal controls, including consideration of improvements made by auditors.

- Internal procedures at the state treasury to safeguard public resources, which comply with applicable laws and regulations. There should be an explicit legal basis for the treasury’s right to use public and IMF funds and for the manner in which those funds are used. Internal policies, procedures, and internal controls should be defined at the state treasury to prevent unauthorized access or use of public resources. Internal

[31] The seven criteria as described by staff are in the staff paper “Safeguards Assessments – Review of Experience,” June 2010, Box 5.

controls would include ensuring there is applicable segregation of duties between those who hold or expend assets, and those who have authority to approve such expenditures.

39. **The Fund and the World Bank have developed and carry out several programs whose data may be leveraged for the purposes of a safeguards assessment of state treasuries: the Fiscal ROSC, Country Financial Accountability Assessments (CFAA), and PEFA.** In fact, the seven criteria listed above are based on Fiscal ROSC indicators, and much of the data could be obtained from Fiscal ROSCs. Staff would need to develop guidelines on how to homogenize the use of ROSC. Existing **CFAA** and PEFA reports could be used to provide supplementary contextual information as needed.

40. **The panel stresses that it would be incumbent upon the staff conducting a safeguards assessment to perform due diligence in ascertaining the quality of existing data from ROSC, CFAA, and PEFA.** The staff should use data already existing from other independent and competent sources. However, where the quality of data cannot be verified, the panel believes it is imperative for the staff to conduct independent data collection before producing its own safeguards report on a state treasury.

41. **In the opinion of the panel, safeguards assessments of state treasuries would need to be performed independently from IMF operations with such entities,** as is the case for assessments of central banks. While some functional departments have business knowledge in the public sector, such as the Fiscal Affairs Department, their work involves both policy advice and technical assistance and, therefore, has an interest at stake in specific system or program implementations. The panel strongly believes that independence of oversight is the cornerstone of a valid safeguards assessment. In this context, therefore, staff conducting assessments of treasuries must have that independent perspective along with specialist experience to be credible. This combination of expertise could be achieved by assembling a safeguards team for fiscal assessments, bringing together the appropriate auditor’s focus on external auditing and internal controls, expertise in the fiscal sector, and independence from specific implementation solutions in a member country.

V. Conclusions

42. **All components of the existing ELRIC framework continue to be relevant, useful, and beneficial.** The staff applies the framework in an effective manner that achieves the objective of the safeguard program.

43. **Given the continuing evolution of central banks, financial markets, and global economies, ELRIC should be continuously improved.** Improvements that should figure more prominently in the next decade include greater focus on central bank governance, risk management, and transparency. Such adaptations would accomplish a strengthening of the

safeguards policy. The panel proposes carefully planned adjustments to the safeguards program to incorporate these recommendations:

- Increased attention to oversight conducted by the board of the central bank. Principles of good governance should be considered including independence, transparency, responsibility, accountability, fairness, discipline, and social responsibility.

- Increased attention to risk management, urging central banks to adopt an integrated risk management framework (IRMF) so they can be better equipped to serve their purpose of providing economic and financial stability.

- Increased transparency of safeguards results, promoting accountability and encouraging corrective actions among central banks. This includes publication of country safeguard assessment reports over a period of time and dissemination of common issues at seminars.

44. **Safeguard assessments should consider policies and procedures in place that facilitate identification of fraud and compliance with laws, regulations, and contracts.** Such policies, including development of an independent whistle-blower policy, have been shown to be effective in heightening fraud detection and safeguarding assets, when properly done.

45. **The panel recommends the Fund conduct safeguards assessments that target state treasuries to achieve the objectives of the safeguard program when loans provide budgetary support.** The panel finds merit in the seven-point framework set forth by staff for conducting these assessments, and notes that existing data could be leveraged so long as due diligence ascertains the quality of the data. The panel also believes that the staff conducting assessments of state treasuries must have both an independent perspective and specialist expertise in the public sector, elements of ELRIC, as well as governance and risk management. Assembling this skill and knowledge set may well require coordination with and assistance from other departments outside the current safeguards team.

46. **Other recommendations the panel believes will contribute to a further improvement in and success of the safeguards program include:**

- Outreach to external auditors, providing education in Fund-specific accounting issues, including international reserves accounting;

- Improved communication internally and externally: to Fund staff, better relating safeguards activities and issues to program design and review, and to central banks, fostering a closer relationship during the monitoring period;

- Inclusion of information technology considerations, looking at how central banks use or move toward using automated accounting and reporting systems.

47. **Finally, the panel supports the Fund's current offering of safeguards assessments on a voluntary basis to member countries not currently seeking resources from the Fund.** Such timing can be beneficial in two ways: central banks can implement recommendations more easily when not under the stress of seeking Fund resources, and having done so facilitates Fund lending to them if needed in the future.

Attachment I. Curricula Vitae of the Panel Members

Dr. Ranee Jayamaha

Dr. Jayamaha is an economist by profession with hands-on experience in central banking, financial system stability, and payment system development. She has had wide experience in advising central banks and financial institutions in the Commonwealth countries, and she is a consultant to the IMF and WB. During her tenure as the Deputy Governor of the Central Bank of Sri Lanka, she chaired a number of national and international policy and operational committees. Dr. Jayamaha has been a member of the Securities and Exchange Commission and the Insurance Board of Sri Lanka. Currently she is the Banking Advisor to His Excellency the President of Sri Lanka.

Work History

Government of Sri Lanka
Banking Advisor to His Excellency the President, May 2009 – present

Central Bank of Sri Lanka (CBSL)
- Deputy Governor, April 2004 – May 2009
- Secretary of the Presidential Commission on Finance & Banking, 1991 – 1993
- Director of the Banking Development Department, 1989 – 1992
- Economist/Senior Economist of the Economic Research Department, 1971 – 1985

Commonwealth Secretariat, London, UK
Special Advisor on Economics, June 1995 – June 2001 (on release by the CBSL)

Ministry of Finance, Sri Lanka
Advisor to the Financial Sector Reform Committee, 1993 – 1995 (on release by the CBSL)

Public and Professional Service

Consultant
- Y2K World Bank Mission, June 1999
- IMF/WB Payment System Development for Bangladesh under the Financial Sector Assessment (FSA) Program, 2003
- WB – Financial Sector Expert for the Assessment of the Financial Sector in the Maldives, 2009 - present

chairperson
- South Asian Association for Regional Co-operation SAARC Payments Council, 2007 – 2009
- Sri Lanka Legal Forum, 2006 – 2009
- Financial System Stability Committee, CBSL, 2004 – 2009
- Credit Information Bureau of Sri Lanka, 2004 – 2009
- Sri Lanka National Payments Council, 2004 – 2009
- Safeguard Assessment Committee, CBSL, 2004 – 2009

Member
- Expert Panel of the Advisory Committee of the G8 Remittances Working Group, 2009 – present
- National Economic Council of Sri Lanka, 2007 – present
- Global Payments Forum, 2002 – present
- Monetary Policy Committee of CBSL, April 2004 – May 2009
- Sri Lanka Insurance Board, April 2004 – May 2009
- Securities and Exchange Commission of Sri Lanka, April 2004 – May 2009
- Working Group on General Payment System Development of the Bank for International Settlements, 2003 – 2005

Publications and Other Professional Contributions

Published in the areas of corporate governance, payment systems development, and regulatory challenges; more than 25 articles in international journals and a large number of articles in local journals and magazines.

Served as a resource person at the following conferences and seminars:

- Sri Lanka/Bangladesh Central Banking Course, 2009 – 2010
- ADB/CBSL International Program, 2009
- Asian Development Bank/World Bank (ADB/WB) International Forum, 2009
- SWIFT International Banking Operations Seminar (SIBOS), 2009 (Hong Kong)
- International Conference on Remittances, 2009 (Rome, Italy)
- Indian Bankers' Association, 2008
- Global Payments Week 2006 (Sydney, Australia), 2007 (Brazil), 2008 (Vienna, Austria)
- Global Payments Conference, 2005 (U.S.A.)

Education

Ph.D. in Monetary Economics, University of Bradford, UK, 1989

MS in Economics, University of Stirling, UK, 1976

BA with honors, University of Peradeniya, Sri Lanka, 1970

Dr. Len Konar

Dr. Konar is a chartered accountant who has been an authoritative contributor to the *King Report on Corporate Governance for South Africa (King III)*. He has been a professor of accounting, and has chaired the External Audit Committee at the IMF and co-chairs the Oversight Panel at the World Bank. He currently serves as a professional director of several companies in South Africa.

Work History

Executive Director
Independent Development Trust, 1992 – 1998
Responsible for internal audit and investment portfolios.

Professor and Head of Accountancy Department
University of Durban-Westville, Chiltern Hills, Durban, South Africa, 1978 – 1992

Public and Professional Service

World Bank
Co-chairman of the Oversight Panel, 2009 – present

International Monetary Fund
Member and Chairman of the external audit committee, 2004 – 2007

National Treasury of South Africa
Chairman of panel to regulate accountants and auditors, leading to publication of Auditing Professions Act, 2005

Government of South Africa
- Chairman of Audit Committee – Department of Defence, 2004 – present
- Chairman of Audit Committee – South African Police Services, 2004 – 2009
- Chairman of Audit Committee – Department of Housing, 2004 – 2008
- Member of Audit and Risk Committees – National Treasury, 2004 – 2007

Professional bodies in South Africa
- Institute of Directors, 2000 – present
- King Committee on Corporate Governance, 1998 – present
- Securities Regulation Panel, 1998 – present

Memberships
- Accounting Standards Board, 2002 – 2007
- Institute of Internal Auditors, 1995 – present
- Independent Regulatory Board for Auditors, 1984 – present
- South African Institute of Chartered Accountants, 1978 – present

Chairman
- Mustek Limited, 2009 – present
- Steinhoff International Holdings Limited, 2008 – present
- Exxaro Limited, 2008 – present

Non-executive director
- Lonmin plc., 2010 – present
- Alexander Forbes Equity Holdings (Pty) Limited, 2008 – present
- Sappi Limited, 2003 – present
- J D Group Limited, 1995 – present
- South African Reserve Bank, 1989 – present

Education and Honors

Honors
- Graduated with Grade Point Average of 5.0 in MAS, awarded Atlantic Richfield Academic Excellence Award
- Best Bachelor of Commerce Graduate, awarded Gold Medal

DCom in Accounting
University of South Africa, Pretoria, 1989

MAS
University of Illinois at Urbana – Champaign, Illinois, USA, 1981

Chartered Accountant (South Africa), *1978*

BCom
University of Durban-Westville, Chiltern Hills, Durban, 1975

Mr. Lynn E. Turner

Mr. Turner has the unique perspective of having been the Chief Accountant of the Securities and Exchange Commission, a member of boards of public companies, a trustee of a mutual fund and a public pension fund, a professor of accounting, a partner in one of the major international auditing firms, the managing director of a research firm, and a chief financial officer and an executive in industry. In 2007, Treasury Secretary Paulson appointed him to the Treasury Committee on the Auditing Profession.

Work History

Chief Accountant
Securities and Exchange Commission (SEC), July 1998 – August 2001

- Served as the principal advisor to the SEC Chairman and Commission on auditing and financial reporting and disclosure by public companies in the U.S. capital markets as well as the related corporate governance matters. These issues included the oversight and development of U.S. auditing, accounting and disclosure standards, as well as matters affecting audit committees of public companies.
- Participated in the international negotiations that led to the creation of the new International Accounting Standards Board and Trustees and worked with the committee that selected the original IASB trustees.
- Worked regularly with Congress, various federal and state government agencies, international regulators, representatives of industry, and the accounting profession.

Senior Advisor
LECG LLC, an international forensics and economic consulting firm, 2009 – present

Kroll Inc., an international risk consulting company, 2003 – 2009

Managing Director of Research and Executive Officer
Glass Lewis & Co., an internationally recognized proxy and financial research firm, 2003 –2007

Professor of Accounting
Colorado State University, 2001 – 2003

Chief Financial Officer and Vice President
Symbios, Inc., an international semiconductor manufacturer, 1996 – 1998

Fellow
Securities and Exchange Commission, 1989 – 1991

Audit and SEC Review Partner
The international audit firm now known as PricewaterhouseCoopers (PWC), 1976 – 1989 and 1991 – 1996

Public and Professional Service

- Provided expert witness testimony before Congress on several occasions.
- Actively involved in the legislative process leading up to passage of the Sarbanes-Oxley Act.
- Provides expert commentary on National Public Radio and all the major television networks including NBC, ABC, CBS, Fox Business News, CNN, CNBC, CNNfn, Bloomberg TV and MSNBC.
- Served on the Standards Advisory Group of the Public Companies Accounting Oversight Board since its inception and now is a member of its newly appointed Investor Advisory Group.
- Served as a member of Financial Accounting Standards Board Investor Technical Advisory Committee.
- Served as the SEC Observer to the FASB Emerging Issues Task Force and Financial Accounting Standards Advisory Council.
- Co-led an investigation of allegations of fraud at the City of San Diego and its pension fund, which gained national attention, February 2005 – August 2006.
- Helped lead the first ever league-wide audit of a major sports league, the National Hockey League, which contributed to the successful negotiation of a new contract between the NHL and players, 2003 – 2004.

Honors

- Named for several years to the list of Top 100 Accountants in the U.S.
- Named to the Directorship100, a list of influential people involved in corporate governance, 2008
- American Accounting Association Exemplar award, 2007
- Numerous articles published; received the Max Block Distinguished Article Award from the New York Society of CPAs, 2006
- National award for Business Information (Accountant) Professional of the Year, awarded from Beta Alpha Psi, the National Accounting Honorary Society, 2001
- Two honorary doctorates in Business Administration: Central Michigan University, May 2000, and Grand Valley State University, October 2000
- Two-time recipient of the SEC Chairman's Award for Excellence, 1999 and 2000
- Alumni of the Year of the Colorado State University College of Business, 1999

Memberships

- Colorado Society of Certified Public Accountants, member
- American Institute of Certified Public Accountants, member
- Financial Executives International, member

Education

MA in Accounting
University of Nebraska, 1976

BA in Business Administration, with a concentration in Accounting
Colorado State University, 1975

ATTACHMENT II. THE PANEL'S SOURCES OF INFORMATION

Fund-specific Reference Material

Folder 1: Background and Modalities for Safeguards Assessments

Issues Note for 2010 review
Terms of Reference for Panel
Operational Guidelines for Safeguards Assessments (issued November 10, 2009)
Safeguards Assessments: Framework for Risk-Based Monitoring
Safeguards Assessments: Facts and Figures
Safeguards Assessments 2006 Update Papers
Safeguards Assessments 2007 Update Papers
Safeguards Assessments 2008 Update Papers
Safeguards Assessments 2009 Update Papers

Folder 2: Previous Reviews Board Papers

2000 Review—Board Paper Strengthening Safeguards on the Use of Fund Resources
2000 Review—Strengthening Safeguards on the Use of Fund Resources—Independent Review of IMF Staff Proposals, EBS/00/30
2000 Review—Summing Up by the Acting Chairman Strengthening Safeguards on the Use of Fund Resources and Misreporting of Information to the Fund-Policies, Procedures, and Remedies-Preliminary Considerations
2002 Review—Board Paper Safeguards assessments Review of Experience and Next Steps, EBS/02/27
2002 Review—IMF Panel of Experts on Safeguards Assessments Review of Experience and Next Steps
2002 Review—The Acting Chair's Summing—Safeguards Assessments, April 1, 2002
2002 Review—Summing Up by the Acting Chairman Revision 1
2002 Review—Press Release IMF Adopts Safeguards Assessments as a Permanent Policy, April 5 2002
2005 Review—Board Paper Review of Experience
2005 Review—Report of the Independent Panel on Safeguards Assessments
2005 Review—The Acting Chair's Summing Up Safeguards Assessments—Review of Experience
2005 Review—Supplement and Proposed Decision, Supplement 1 December 1, 2005 [Covers the sharing of Safeguards Assessment reports with other international agencies]
2005 Review—Supplement correction
2005 Review—Supplement Press release Safeguards Assessment Reports

Folder 3: Confidential Safeguards Reports

Dem Republic of Congo --January 2008 Report
Liberia--June 2007 Report
Liberia -- August 2008 Report
Seychelles -- December 2008 Report
Tanzania -- August 2008 Report
Tanzania -- November 2009 Report
Cambodia -- January 2004 Report
Cambodia -- January 2010 Report
Nepal -- October 2004 Report
Sri Lanka -- July 2003 Report
Sri Lanka -- July 2009 Report
Iceland -- July 2009 Report
Latvia--July 2009 Report
Ukraine--July 2004 Report
Ukraine -- April 2009 Report
Moldova -- October 2006 Report
Afghanistan -- June 2006 Report
Afghanistan -- March 2008 Report
Georgia -- December 2004 Report
Georgia -- December 2008 Report
Mauritania -- May 2004 Report
Mauritania -- April 2007 Report
Pakistan -- February 2001 Report
Pakistan -- March 2009 Report
Costa Rica -- July 2009 Report
Guatemala -- August 2002 Report
Guatemala -- September 2009 Report
Paraguay -- January 2003 Report
Paraguay -- October 2006 Report
Colombia --August 2009 Report for FCL arrangement

Safeguards Reports provided later under separate cover

The Gambia -- 2004, 2006, and 2009 Reports
Ghana -- 2003, 2009 Reports
Latvia -- 2001 Report

Reports Obtained from IMF.org and Related Sites

PEFA Framework Guidelines and selected country PEFA reports
Selected country Article IV staff reports
Selected country CFAA reports
Selected country ROSC reports

Other International Sources

Sources on Governance

Corporate Governance and the Financial Crisis: Key Findings and Main Messages, Organization for Economic Co-operation and Development, 2009.

CLSA Asia-Pacific Markets. <www.clsa.com> 22 June 2010.

Financial Reform: A Framework for Financial Stability. Group of Thirty, 2009.

"The IMF and Good Governance." IMF Factsheet, 5 April 2010.

Implementation Plan for Strengthening World Bank Group Engagement on Governance and Anticorruption. World Bank, 2007.

Improving Financial Regulation: Report of the Financial Stability Board to the G20 Leaders. Financial Stability Board, 2009.

Internal Control: Guidance for Directors on the Combined Code [Turnbull Report]. The Institute of Chartered Accountants in England & Wales, 1999.

King Report on Corporate Governance for South Africa (King II and III). Institute of Directors of Southern Africa, 2002 and 2009.

Leaders' Statement: The Pittsburg Summit. Group of Twenty, 2009.

Principles of Corporate Governance. Organization for Economic Co-operation and Development (OECD), 2004.

Report to the Nations on Occupational Fraud and Abuse. Association of Certified Fraud Examiners, 2010.

Strengthening World Bank Group Engagement on Governance and Anticorruption: Second Year Progress Report. World Bank, 2009.

"Towards Greater Protection of Whistleblowers." Transparency International. <http://www.transparency.org/global_priorities/other_thematic_issues/towards_greater_protection_of_whistleblowers> 22 June 2010.

Sources on Risk Management

Enterprise Risk Management—Integrated Framework. Committee of Sponsoring Organizations (COSO), 2004.

High Level Principles of Risk Management. Committee of European Banking Supervisors (CEBS), 2010.

ISO 31000 Risk Management: Principles and Guidelines. International Organization for Standardization (ISO), 2009.

Sources on Transparency

"About Transparency International." <http://www.transparency.org/about_us> 24 June 2010.

"Code of Good Practices on Fiscal Transparency." IMF, 1998.

"Code of Good Practices on Transparency in Monetary and Financial Policies: Declaration of Principles." IMF, 26 September 1999.

"Transparency at the IMF." IMF Factsheet, 8 January 2010.

Central Banks Consulted

1. The panel held conferences with the following central banks.

Central Bank	**Authorities in Attendance**
Central Bank of The Gambia (teleconference, April 1, 2010)	Mr. Saho, Governor
Bank of Ghana (teleconference, March 22, 2010)	Mr. Arthur, Governor Mr. Wampah, Deputy Governor Mr. Adu, Internal Auditor Mr. Sai, Head of Banking Supervision Department
Bank of Latvia (teleconference, March 24, 2010)	Mr. Kalis, Chairman of the Board Mr. Caune, Chief Accountant Mr. Asmanis, Head of Internal Audit
State Bank of Pakistan (videoconference, March 24, 2010)	Mr. Azeemi, Assistant Director Mr. Riazuddin, Chief Economic Advisor Mr. Qureshi, Executive Director of Internal Audit & Compliance Department Mr. Rasheed, Comptroller of Finance Ms. Bakhtiar, General Counsel Mr. Khan, Director of Finance Department Mr. Bakhsh, Head of Financial Accounts Division, Finance Department

Staff Consulted

2. The panel met in person with Fund staff from area and functional departments on March 25 and 26, 2010. Departments represented were AFR. APD, EUR, FAD, FIN, LEG, MCD, SPR, WHD. Mr. Turner, panel chair, held an additional follow-up meeting in person with FAD on April 12, 2010.

3. The panel also met in person with World Bank staff members Mr. James Brumby and Mr. A. Hega on March 26, 2010 to discuss the Public Expenditure and Financial Accountability (PEFA) partnership.

Offices of Executive Directors Consulted

4. Three separate assemblies of personnel from the offices of executive directors met with the panel. Offices were represented variously by executive directors, alternates, or advisors.

ATTACHMENT III. SUMMARY OF MEETINGS

Views from Central Banks

1. **The topics of discussion with central banks included**: (i) clarity of the purpose of the safeguards policy, (ii) effectiveness of safeguards assessments and monitoring in achieving the policy objectives, (iii) usefulness of the safeguards activities to the central bank's operations and its management, (iv) value of the safeguards seminars, (v) adequacy of the ELRIC framework to assess issues related to governance and risk management, (vi) the authorities' views on transparency, (vii) appropriateness of safeguards recommendations, priorities, and deadlines, (viii) sufficiency of communication with the safeguards staff, (ix) the authorities' views on extending safeguards assessments beyond their current association with Fund arrangements, to be conducted proactively with all Fund members, and (x) practicality of having central banks employ a safeguards template for self-assessments.

2. **The central banks consulted are approving of the safeguards policy and acknowledge its benefits.** They appreciate that the safeguards exercise has better aligned them with best practices. They recommend the process to other central banks, even outside the context of a pending financial arrangement with the Fund.

3. **All agreed that risk management (RM) and governance require and warrant focused attention.** Their opinions varied on whether RM and governance are adequately covered by ELRIC. They tended to see the current safeguards framework as addressing risk management in a silo fashion. A few tended to equate risk management with audit controls, one recognized the need for an integrated risk management framework that applies to the whole organization, and another identified its key risk concerns as more strategic in nature: the financial risks of managing reserves on behalf of the state and conducting investment activities, and the operational risks of money transfers and the types of transactions being undertaken in financial markets.

4. **Views on transparency of safeguards information varied widely.** Some central banks are concerned about their own reputational risk if information is irresponsibly represented in the press. Conversely, one stated that the publication of safeguards results would begin a dialog in the public arena, and if handled well, this dialog would be a healthy development.

5. One bank stated that the independent auditors do not always appear to be knowledgeable of the operations of the banks, particularly with respect to reserves. (This opinion was also voiced by staff members.)

Views from Offices of Executive Directors

6. **The panel queried the offices of the EDs regarding:** (i) their appraisal of the value and effectiveness of the current safeguards policy and its possible extensions to the ELRIC framework to include governance and risk management, (ii) their judgment about expanding safeguards to treasuries when resources for budgetary support are at stake, and (iii) their views on transparency for safeguards information.

7. **The offices expressed general satisfaction with the safeguards policy, believing it to be helpful in reducing risk to the Fund and protecting its reputation.** Concerns mentioned include the cost/benefit ratio for the policy and any proposed extensions, and the need to continually fine-tune the policy to adapt to newly emerging risks. There was strong agreement that a focus on governance is essential to help guard against fraud at the top. Risk management was seen as something that would be heavily influenced by the country-specific context, such as political stability, external audit quality, and the ethics of central bank authorities.

8. **Many expressed the position that it is not acceptable to neglect safeguards assessments of treasuries, although they acknowledged the logistical difficulties of doing so.**

9. **Views on transparency varied widely.** There was much discussion about the specifics of what would be published and by whom, what purpose would be served, and how various member countries may react.

Views from Staff

10. The discussion topics for staff were the same as those for offices of EDs as well as (i) the practicality of safeguards recommendations for particular member countries, and (ii) the feasibility of whistle-blowing policies.

11. **Staff members in general are supportive of the safeguards policy and believe it is a worthwhile undertaking.** They indicate that most member countries respond well to it, seeing the inherent benefit to them. A concern expressed is that safeguards assessments can only identify procedures that *if properly followed* would safeguard resources; assessments do not always ascertain whether procedures are properly followed. The goal should be to strengthen safeguards and learn to identify, prevent, and mitigate fraud based on lessons learned from past incidents. Economists for some countries see the safeguards policy as a bureaucratic hurdle whose findings and recommendations are tangential to the countries' economic problems and solutions.

12. **Staff members substantiated the importance of assessing governance to help guard against fraud.** They noted the difficulty in assessing and addressing the "tone at the

top," however, because of its subjectivity and sensitivity. Suggestions included having the safeguards framework specify fit and proper requirements for a central bank governor. A thorough examination of rules and procedures of operation should reveal the tone at the top.

13. **Functional departments demonstrated keen interest in developing a practical methodology for safeguarding Fund resources used for budgetary support.** Concerns about the complexity of the fiscal sector were expressed, but there was acknowledgement that there is currently a serious gap in safeguards for not looking into state treasuries.

14. **Staff members expressed a positive, though cautious, response to the question of increased transparency of safeguards information.** They cited that donor countries sometimes want to know such information, and countries who have shown significant improvement want to publish the information. One view was that too much transparency too soon in the safeguards cycle for a country could result in a political matter and be counterproductive. Some staff members questioned the usefulness of publishing the entire safeguards report, considering that it may be too technical and detailed to be of any benefit in the public domain, but conceded that published summaries and results by country could be useful. It is important to focus on whether publication advances the purpose of the safeguards policy and whether the information is good for the Fund and its member countries.

15. **Area departments expressed the need for more sensitivity toward country differences and flexibility in applying the safeguards policy.** Factors to consider are the size and sophistication of the country, the size and type of arrangement being sought, whether the bank is in need of improved credibility, the political climate in the, any special cultural conditions, and the effects of recommendations on multiple member countries in a regional bank . The cost of implementing safeguards recommendations, which rests with the central banks, can be a formidable burden to some countries (Liberia was cited). They urged that the safeguards policy needs to strike a reasonable balance, in cooperation with the central banks, between pushing for progress and understanding the country's limitations.

16. **Area departments cautioned that some cultures would not be receptive to a whistle-blowing policy.**

17. In a meeting with the staff of the Safeguards Assessments Division, the panel learned how safeguards data are tracked in a database application, and the nature of feedback and pushback that staff receives on draft safeguards reports. The panel also obtained the staff's perspectives on ELRIC, governance, and risk management; the feasibility of creating a safeguards template for self-assessment purposes, and problems encountered with some external auditors arising from the auditors' lack of knowledge in macroeconomics and central bank accounting.

18. In meetings with senior staff of FIN, the panel and FIN exchanged perspectives on the key issues for this year's policy review. The panel briefed FIN on results of the discussions with central banks, Fund executive directors and advisors, and Fund staff.

ATTACHMENT IV. SDR VALUE OF FUND ARRANGEMENTS SINCE INCEPTION OF SAFEGUARDS

In Table 1, data for the years 2001 – 2009 are taken from the Fund Annual Report 2009. For 2010, data are taken from the Quarterly Financial Statement of January31, 2010. These data are the referred to in the body of this report, paragraph 5.

Table 1. Number and SDR Value of Fund Arrangements, 2001-2010

Financial Year	Number of New and Augmented Arrangements	Amount committed (in millions of SDRs)
2001	26	14,333
2002	18	41,287
2003	22	30,571
2004	15	15,486
2005	14	1,713
2006	13	8,474
2007	12	600
2008	8	1,333
2009	28	66,736
2010*	29	44,141
TOTAL	**185**	**224,674**
* 2010 figures represent a 9-month period ending 1/31/10.		

ATTACHMENT V. RISK-BASED MONITORING

Figure 1 shows the required and conditional tools to use in each monitoring intensity level. To use a tool with no marker requires FIN management approval.

Figure 1. Monitoring Tools by Monitoring Intensity Level

	----------------Monitoring Intensity Silos-------------			
Monitoring Tools	**Low**	**Medium Low**	**Medium High**	**High**
	Refer Explanatory Notes overpage			
Desk reviews of financial statements, management letters, staff reports/briefs, and other relevant sources	✔	✔	✔	✔
Contacts with area department	✔	✔	✔	✔
Contacts with central bank	✔	✔	✔	✔
Discussions with external auditor	∮	✔	✔	✔
Review of internal audit reports pertinent to areas of interest to safeguards		∮	✔	✔
Discussions with functional departments/ TA experts		∮	✔	✔
Meetings at HQ with Governor/Deputy Governor or other senior staff (at IMF Spring or Annual meetings)			∮	✔
On site staff visits (see note 5)			∮	✔
Contacts with external agents (e.g., auditor general, audit committee, ministry of finance, etc.)			∮	∮
Analysis of information from World Bank/IFI reports (CFAA/RAMP/ROSC/FSAP)			∮	∮
Formal letter from IO to authorities			∮	∮
Special reviews by external experts				∮
Proposals to introduce program conditionality or special measures (e.g., SDR account)				∮
Contact with Executive Director's office				∮
On-site Monitoring Assessments (see note 6)				∮
Note to Management				

Attachment VI. Principles of Good Governance

CORPORATE GOVERNANCE

The following can be regarded as constituting the seven characteristics of good corporate governance. Adapted from CLSA Emerging Markets, and the King Code and Report on Corporate Governance for South Africa (King II and III).

1 Discipline

Corporate discipline is a commitment by the Bank's senior management to adhere to behaviour that is universally recognised and accepted to be correct and proper. This encompasses the Bank's awareness of, and commitment to, the underlying principles of good governance, particularly at senior management level.

2 Transparency

Transparency is the ease with which an outsider is able to make meaningful analysis of the Bank's actions, its economic fundamentals and the non-financial aspects pertinent to its activities. This is a measure of how good management is at making necessary information available in a candid, accurate and timely manner - not only the audit data but also general reports and press releases. It reflects whether or not stakeholders and interested parties obtain a true picture of what is happening inside the Bank.

The board should disclose information in a manner that enables stakeholders to make an informed analysis of the Bank's performance, and sustainability.

3 Independence

Independence is the extent to which mechanisms have been established to minimise or avoid potential conflicts of interest that may exist, such as dominance by a strong Governor or the Treasury or the Minister of Finance. These mechanisms range from the composition of the board, to appointments to committees of the board, and external parties such as the auditors. The decisions made, and internal processes established, should be objective and not allow for undue influences.

4 Accountability

Individuals or groups in the Bank, who make decisions and take actions on specific issues, need to be accountable for their decisions and actions. Mechanisms must exist and be effective to allow for accountability. These provide stakeholders with the means to query and assess the actions of the board and its committees.

The board should be able to justify its decisions and actions to lenders and other stakeholders.

5 Responsibility

With regard to management, responsibility pertains to behaviour that allows for corrective action and for penalizing mismanagement. Responsible management would, when necessary, put in place what it would take to set the Bank on the right path. While the board is accountable to the Bank, it must act responsively to and with responsibility towards all stakeholders of the Bank.

The board should assume responsibility for the assets and actions of the Bank and be willing to take corrective actions to keep the Bank on a strategic path that is ethical and sustainable.

6 Fairness

The systems that exist within the Bank must be balanced in taking into account all those that have an interest in the Bank and its future. The rights of various groups have to be acknowledged and respected.

The board should ensure that it gives fair consideration to the legitimate interests and expectations of all stakeholders of the Bank.

7 Social Responsibility

A well-managed Bank will be aware of, and respond to, social issues, placing a high priority on ethical standards. A good corporate citizen is increasingly seen as one that is non-discriminatory, non-exploitative, and responsible with regard to environmental and human rights issues. A Bank is likely to experience indirect economic benefits such as improved productivity and corporate reputation by taking those factors into consideration.