

**LAPSE OF
TIME**

EBAP/16/102

November 9, 2016

To: Members of the Executive Board

From: The Secretary

Subject: **Proposed Amendment to the Terms of Reference of the External Audit Committee**

Board Action:	Executive Directors' consideration on a lapse of time basis
Deadline to Request a Board Meeting, after which Proposed Decision Deemed Approved:	Wednesday, November 16, 2016 12:00 (noon)
Proposed Decision:	Page 7
Publication:	Publication of the paper is not proposed. However, it is proposed that the revised terms of reference (ToR) be published on the public website.



November 9, 2016

PROPOSED AMENDMENTS TO THE TERMS OF REFERENCE OF THE EXTERNAL AUDIT COMMITTEE

EXECUTIVE SUMMARY

The External Audit Committee (EAC) is an important element of the Fund's governance structure. The committee comprises three external experts and provides general oversight of the Fund's annual audit. The committee is guided in its work by the Fund's By-Laws and Rules, as well as its terms of reference (ToR), which were adopted by the Executive Board in 1999.

Under the ToR, the EAC "shall review its terms of reference periodically and may recommend amendments for consideration by the Executive Board." The practices of the EAC have evolved since adoption of the original ToR and in its 2015 report to the Executive Board, the EAC recommended a review and update of the ToR.

Staff has assisted the EAC in the review, including the preparation of draft revisions to the ToR. These draft revisions reflect changes in the Fund's audit framework, evolving practices of the EAC, and have been informed by a review of current professional guidance for audit committees, as well as the terms of reference of comparator international financial institutions. The draft revised ToR were circulated to Executive Directors as a supplement to the 2016 EAC report ahead of the EAC briefing of the Board in July 2016. The EAC now seeks formal consideration and approval of the draft revised ToR by the Executive Board. Staff fully supports the recommended amendments.

Approved By
Andrew Tweedie (FIN)

Prepared by the Finance Department in Consultation with the External Audit Committee and the Legal Department.

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INTRODUCTION

1. The External Audit Committee (EAC) is an important element of the Fund's governance structure. The committee comprises three external experts and provides general oversight of the Fund's annual audit. The legal basis for the establishment and operation of the committee is provided under Section 20 of the Fund's By-Laws, Rules J-6 through J-8 of the Fund's Rules and Regulations, and the EAC terms of reference (ToR), which were adopted by the Executive Board in 1999 (see also Annex II).¹ The committee was initially established in 1947, and its role, functions, and procedures have evolved over the years (see Annex IV). Under Section 20 (c) of the Fund's By-Laws, the EAC may propose changes to the ToR for approval by the Executive Board, and the ToR provide that the EAC "shall review its terms of reference periodically and may recommend amendments for consideration by the Executive Board."

2. In its 2015 report, the EAC recommended a review and update of the EAC ToR, which have not been amended since their adoption in 1999.² The report also invited the Board to consider extending the scope of the EAC's mandate beyond the current ToR focus. At the 2015 EAC Board briefing, there was broad support to update the ToR, whereas views on the extension of scope of EAC's responsibilities were mixed. The EAC subsequently decided to focus its review on updating and benchmarking the EAC's ToR against existing practices. It was agreed that the broader issue of extending the scope of the EAC's mandate required further thought and could be revisited at a later stage, if warranted.

3. Following the EAC's recommendation, staff assisted the EAC in the review and the preparation of a draft revised ToR, which were circulated by the EAC to the Executive Board in the context of the July 2016 EAC briefing. The draft revised ToR are informed by the results of a benchmarking exercise against current best practices of audit committees, as well as a review of the terms of reference of audit committees at comparator international financial institutions. Although there is no substantive change in the scope of the EAC's current responsibilities, the proposed revisions reflect developments in the Fund's audit framework, evolving EAC work practices, and contain clarifications regarding its mandate as a result of the benchmarking exercise. During the July 2016 EAC briefing to the Board, Directors had no comments on the draft revised ToR.³ The EAC now seeks formal approval by the Board of the draft revised ToR, which are identical to those presented to the Board in July.

4. This paper discusses the proposed revisions to the ToR, and seeks approval by the Executive Board of a revised ToR as proposed by the EAC. It starts with background on the establishment of the initial ToR, describes the basis for the current review, and highlights the key

¹ *The Fund's External Audit Function—Terms of Reference for the External Audit Committee* (EBS/99/137, 7/23/1999).

² *Report of the External Audit Committee to the Executive Board* (EBAP/15/57, 6/24/2015).

³ *External Audit Committee—Revised Draft Terms of Reference* (EBAP/16/66, Supplement 1, 7/11/2016).

proposed changes. The draft revised ToR included in Annex I are recommended by the EAC and staff, and proposed by the EAC for approval by the Executive Board.

INITIAL TERMS OF REFERENCE

5. The current oversight role of the EAC was established in 1999, as a result of an independent review of the Fund's audit function.⁴ Prior to 1999, the EAC was entrusted with conducting the audits of the IMF's financial statements. Although the EAC was assisted in its work by an external audit firm, the audit opinions were signed by the EAC. On the recommendation of the 1997 EAC, the Fund solicited a review of its external audit function by an independent expert.⁵ As a result of this review, the EAC's role transitioned from conducting the audits to providing oversight. The external audit firm assumed full responsibility for conducting the audits and signing the audit opinions in 2000.

6. The new oversight responsibilities of the EAC were reflected in the initial ToR adopted in 1999. These ToR were prepared by management and approved by the Executive Board and specified that future revisions to the ToR could be proposed by the EAC for approval by the Board. Implementation of the new roles of the EAC and the external audit firm required amending provisions in the Fund's audit framework as set out in the Fund's By-Laws. The initial ToR came into effect after approval of the amended By-Laws by the Board of Governors on September 30, 1999.

BASIS FOR REVISIONS TO THE TOR

7. Consistent with recommendations by the EAC in its 2015 report to the Executive Board, the proposed revisions to the ToR incorporate developments in the audit framework including Board decisions and evolving practices of the EAC since 1999 (see Annex IV). As noted in the EAC report, the current practices of the EAC are not fully captured by the existing ToR. In particular: (i) the EAC's oversight has extended to some areas and departments not explicitly mentioned in the ToR; (ii) the number and length of visits have exceeded those prescribed in the ToR; and (iii) reporting to the Board has evolved. Some practices have changed due to Board decisions adopted since 1999 (see Annex IV for further details), while other changes resulted from the evolving best practices of audit committees. The proposed revised ToR reflect these various developments.

⁴ *Independent Review of the Fund's Audit Functions—Terms of Reference* (EBD/98/44, May 18, 1998) and *Review of the Fund's External Audit Function* (EBS/99/23 March 1, 1999).

⁵ The review was conducted by Mr. Eccles, the then Chairman of the International Accounting Standards Advisory Council and former Vice President and Controller of the World Bank.

8. The revisions draw on a benchmarking exercise performed by staff. The exercise constituted a comparative review of the audit committee charters of other international financial institutions and audit committee guides issued by established professional bodies.⁶

- The review found that the EAC's existing ToR were generally in line with best practices and no major overhaul of the ToR was needed. For example, the EAC composition meets or exceeds requirements of comparator charters and guides since all three EAC members are independent and are financial experts. Also the EAC scope of work covers all key areas typically assigned to audit committees, and the EAC practices include executive sessions with the external audit firm and internal auditors—an important requirement of all comparator charters and guides.
- In some areas, differences between the EAC's existing ToR and comparator charters and guides stemmed from the Fund's specific governance structure. For example, most comparators, whose audit committee members are comprised of Board members, require the audit committee to appoint the external audit firm. At the Fund, given the composition and advisory role of the EAC, this responsibility belongs to the Executive Board, which selects the audit firm in consultation with the EAC.
- In a number of areas, however, potential improvements were identified to clarify the EAC's roles and responsibilities or to update language with the terminology used by comparators. For example, the first section of the ToR now clearly lays out the respective roles and responsibilities of the EAC, the external audit firm, management, and the Office of Internal Audit and Inspection (OIA). For each new or modified provision in the draft revised ToR, Annex III provides a snapshot of similar provisions in the comparator organizations' charters and guides.

9. The revisions also include new provisions on avoidance of conflicts of interest. In carrying out their oversight role, it is understood that the EAC members should protect confidential information provided to them, maintain their independence and refrain from any action that could give rise to an actual or perceived conflict of interest. In June 2016, staff issued a paper proposing a new approach to mitigate risks of conflict of interest, which was endorsed by the Board.⁷ The proposed revisions incorporate a section on conflicts of interest in line with the approach endorsed by the Board.

⁶ The international financial institutions selected for benchmarking are: the United Nations Development Program (UNDP); the European Central Bank (ECB); the World Bank (WB); the Inter-American Development Bank (IADB); the Asian Development Bank (ADB); the European Investment Bank (EIB); and the Bank for International Settlements (BIS). The audit committee guides used in the study are: *"Global Public Sector Insight: Independent Audit Committees in Public Sector Organizations"* by the Institute of Internal Auditors (IIA); *"The AICPA Audit Committee Toolkit: Government Organizations, 2nd edition"* by the American Institute of Certified Public Accountants (AICPA); and *"Guidance on Audit Committees 2012"* by the UK Financial Reporting Council (UK).

⁷ *Selection of Member of the External Audit Committee and Approach to Conflict of Interest Mitigation for EAC Members* (EBAP/16/62, June 21, 2016).

KEY PROPOSED CHANGES

10. Taking into account the comparative analysis and evolving practices of audit committees, the proposed changes to the ToR fall into three broad categories: (i) aligning the content with best practices of audit committees; (ii) providing greater flexibility on work modalities; and (iii) clarifying the scope of the EAC's oversight responsibilities. Changes proposed in each of these categories are outlined below.

11. Revisions are proposed to align the ToR with current best practices of audit committees:

- The “responsibilities” section has been expanded to describe key tasks performed by the EAC in each oversight area. The tasks in the proposed ToR largely reflect how existing practice has evolved during EAC visits, and also incorporate specific tasks that the EAC has agreed to take on, such as the review of consulting services provided by the external audit firm (see Annex IV).
- A new requirement has been introduced for the EAC to regularly assess its effectiveness and any need for changes in its work plan or processes. This requirement is present in most comparator charters and in all guidance documents that staff reviewed. This self-evaluation will be an important element in maintaining and strengthening the EAC's effectiveness. Although this is a new requirement, in practice, the current EAC has been reviewing its effectiveness during the final visit each year.
- The EAC's responsibility for establishing its annual work plan has also been made explicit. While the EAC currently determines its agenda and meetings, developing an annual work plan will provide an opportunity to plan the allocation of the EAC's time to ensure sufficient coverage of the key areas in the most efficient manner during the year.

12. The proposed revisions also provide flexibility in areas where the existing ToR, particularly as regards work modalities, were unnecessarily prescriptive. The current ToR were unduly prescriptive on procedural matters, such as the timing, number and expected length of the EAC visits. Flexibility is needed to allow the EAC to make adjustments based on its work plan. In this connection, the draft revised ToR give the EAC greater discretion to formulate its work modalities.

13. Changes have also been introduced to clarify the scope of the EAC's oversight. The draft revised ToR include greater specificity as to the aspects of the financial statements and external audit processes the EAC will review. Similar additional detail is also included for the review of internal audit and internal controls. Moreover, the draft revised ToR reframes the EAC's role in risk management under “Oversight of other audit-related issues”, consistent with the current EAC involvement in this area.

14. The EAC recommends the revised ToR as set forth in Annex I for consideration and approval by the Executive Board. Staff fully supports the recommended changes.

Proposed Decision

The following decision, which may be adopted by a majority of votes cast, is proposed for adoption by the Executive Board:

“The Executive Board approves the revised terms of reference for the External Audit Committee appointed under Section 20 of the By-Laws, as set forth in the Annex I to EBAP/16/102.”

Annex I. Revised Terms of Reference Proposed by the EAC

External Audit Committee Terms of Reference

These Terms of Reference of the External Audit Committee (EAC) are adopted under the authority of Section 20 of the By-Laws, and are supplementary to its provisions and to Rules J-6 through J-8 of the Rules and Regulations of the International Monetary Fund. They also incorporate relevant Board decisions.

1. Purpose

The EAC has general oversight responsibilities for the financial statements annual audit. The responsibility for performing the external audit and issuing the audit opinions rests with the external audit firm. Management is responsible for preparing the financial statements and designing, implementing, and maintaining the system of internal controls. The Office of Internal Audit and Inspection provides independent objective assurance and consulting advice in relation to the Fund's activities as a whole, and maintains a functional reporting relationship with the EAC.

In order to discharge its oversight responsibilities, the EAC shall in particular consider the financial reporting practices, the external audit framework, the system of internal controls, and the internal audit framework, as further specified in paragraph 2 below, and take up such other issues that it considers relevant for the fulfillment of its general oversight responsibilities.

2. Specific Responsibilities

Financial and related reporting practices

2.1 Review and discuss with staff and the external audit firm major issues regarding accounting principles and financial statement presentation, including critical accounting policies, practices, and assumptions, and any changes in them; decisions requiring a significant amount of judgment; the extent to which the financial statements are affected by any unusual transactions in the year and how they are disclosed; the clarity of disclosures; significant adjustments arising from the audit; and compliance with accounting standards.

External audit framework

2.2 Review the selection procedures for an external audit firm, which shall be selected by the Executive Board, in consultation with the EAC, and appointed by the Managing Director. As part of the consultation with the EAC prior to the selection of a new external audit firm, the EAC shall provide its view on whether existing consulting contracts of an audit firm could compromise the external audit firm's independence if it were to be selected as the external audit firm.

2.3 Review and discuss with the external audit firm and staff of the IMF the audit approach of the external audit firm. For this purpose, the EAC shall receive a written submission of the external audit firm's audit plan. Discuss with the external audit firm the external audit results, including the external audit firm's opinions, its comments on controls and other observations, and any restrictions on the scope of the audit.

2.4 Meet privately with the external audit firm to discuss audit-related topics in confidence.

2.5 Review the external audit firm's representation of its independence, including the fees related to any consulting services it provides to the IMF during its engagement as the external audit firm, and the nature of the services provided. Review the external audit firm's representations of compliance with International Standards on Auditing.

2.6 Evaluate the external audit firm's performance based on reports received from the external audit firm describing internal quality control procedures and issues raised by control, peer, or supervisory reviews, private sessions with the external audit firm, and input from those with substantial interactions with the audit firm.

System of internal controls

2.7 Discuss with the external audit firm and staff of the IMF the key risks that could impact the audit and the related system of internal controls, including the environment in which the system operates.

2.8 Review any significant operational, internal control, or reporting risks or issues affecting the financial statements that arose during the course of the audit and monitor their resolution or follow up.

2.9 Discuss the system and practices established by the IMF to promote ethical standards and enable staff to confidentially and anonymously report issues.

Internal audit framework

2.10 Review and approve the Office of Internal Audit and Inspection's charter and discuss steps taken to ensure adherence to the International Standards for the Professional Practice of Internal Auditing.

2.11 Review the Office of Internal Audit and Inspection's annual plan and monitor its execution.

2.12 Review the results and quality of the audits performed by the Office of Internal Audit and Inspection, its written reports concerning the scope of reviews of compliance, any significant findings, and the resolution and follow-up on findings and recommendations.

2.13 Review the effectiveness of the Office of Internal Audit and Inspection in discharging its responsibilities.

2.14 Maintain direct communication, and meet privately at least annually, with the Office of Internal Audit and Inspection Director.

Oversight of other audit-related issues

2.15 The EAC may take up such other issues as it considers relevant for the fulfillment of its general oversight responsibilities, which may include briefings on the status of one-off projects with significant financial reporting impact and developments in risk management issues, taking into account the role of other oversight mechanisms and governance in place.

3. Confidentiality and conflict of interest

3.1 The EAC shall have access to information in possession of the IMF as needed to carry out its function, including having access to members of management, Executive Directors, and staff and to relevant documents and records.

3.2 Members of the EAC undertake to protect the security of any confidential information provided to, or generated by, the IMF, in line with the existing policies of the IMF and requirements included in their appointment and reaffirmation letters. In particular, members of the EAC shall not divulge to persons or bodies external to the IMF, or otherwise misuse, any information of a confidential nature that comes to their attention in the course of the performance of their duties and should not use any information obtained in the course of the performance of their duties for personal gain.

3.3 The EAC members should maintain their independence throughout their appointment, and avoid any situation involving a conflict, or the appearance of a conflict, of interest with the IMF or the IMF's external audit firm and the performance of their official duties.

4. Work modalities

Work procedures

4.1 Each EAC shall determine its own procedures.

4.2 In cases where the EAC is asked to review a matter or provide its view, the Chairman shall convey the position of the committee, including dissenting views for cases in which there is no consensus in the EAC.

Work plan

4.3 The EAC shall establish its own work plan. It is expected that the EAC will meet at least three times a year, and each EAC member is expected to attend each meeting in person. Additional meetings may also be organized through the use of any appropriate means of communication when the circumstances require. The members of the EAC shall be available for consultation on emerging

audit matters throughout the year, including informal meetings or briefings provided by staff through teleconference.

4.4 During its visits, the EAC is expected to meet with IMF staff to discuss developments relevant to its areas of oversight. The EAC may also hold informal meetings with Board members.

EAC effectiveness and training

4.5 The EAC should regularly assess, with relevant inputs, the need for changes in the EAC's work plan or processes.

4.6 A new member of the EAC should be available for orientation from the IMF to prepare for the role of an EAC member. The EAC members are expected to stay abreast of developments in accounting, auditing, and other areas relevant to their general oversight responsibilities.

5. Reporting to the Executive Board and the Board of Governors

5.1 At the conclusion of its work related to a particular financial year, the EAC should prepare and circulate to the Executive Board a formal activity report covering its work conducted during the year and any recommendations it may have for consideration by the Executive Board.

5.2 The EAC shall give the Executive Board a briefing on the results of its oversight work, and may provide interim briefings as deemed appropriate.

5.3 The EAC shall transmit the external audit reports issued by the external audit firm to the Board of Governors, through the Managing Director and the Executive Board.

6. Amendment to the Terms of Reference

In accordance with the provisions of Section 20(c) of the By-Laws, the EAC shall review its terms of reference periodically and may recommend amendments for consideration by the Executive Board.

Annex II. Current Terms of Reference

External Audit Committee Terms of Reference

These Terms of Reference of the External Audit Committee (EAC) are adopted under the authority of Section 20 of the By-Laws, and are supplementary to its provisions and to Rules J-6 through J-8 of the Rules and Regulations of the International Monetary Fund.

1. Purpose of the EAC

The EAC has general oversight responsibilities for the external audit function within the IMF. The EAC shall review the financial statements of the IMF and the accounts administered by the IMF, including the staff retirement plans, the related financial reporting practices, and the system of internal controls, including the audit process. The responsibility for performing the external audit and issuing the audit opinion rests with the external audit firm. The EAC shall transmit the external audit reports issued by the external audit firm to the Board of Governors, through the Managing Director and the Executive Board.

2. Responsibilities

Financial and Related Reporting Practices

- 2.1 Review the interim and annual financial statements of the IMF and the accounts administered by the IMF, including the staff retirement plans, the external audit firm's opinion, and its comments on controls and other observations. The EAC shall also review the underlying accounting principles with staff of the IMF and the external audit firm.
- 2.2 Review the selection procedures for an external audit firm which shall be selected by the Executive Board, in consultation with the EAC, and appointed by the Managing Director.
- 2.3 Review and discuss with the external audit firm and staff of the IMF the scope and content of the external audit firm's examination, and the coordination with the Office of Internal Audit and Inspection. For this purpose, the EAC shall receive a written submission of the external audit firm's audit plan.
- 2.4 Review any significant operational or reporting issues affecting the financial statements which were discussed by Fund management and the external audit firm, monitor the external audit results, and review the external audit firm's performance.
- 2.5 Meet separately with the external audit firm to discuss pertinent matters, including the Fund's accounting principles as applied to its financial reporting, and any restrictions on the scope of the audit.

System of Internal Control

- 2.6 Review with the external audit firm, the Office of Internal Audit and Inspection, and staff of the Treasurer's Department, risk management within the IMF and the system of internal controls, including the environment in which the system operates.
- 2.7 Review the adequate discharge by the Office of Internal Audit and Inspection of its responsibilities by reviewing and approving the Office of Internal Audit and Inspection's charter and reviewing its plans, the results and quality of its audits, and its adherence to standards of internal auditing.
- 2.8 Review the Office of Internal Audit and Inspection written reports concerning the scope of reviews of compliance, any significant findings, and the resolution and follow-up on findings and recommendations; maintain direct communication with the Office of Internal Audit and Inspection Director; and meet privately with the Director at least annually.

Reporting Responsibilities

- 2.9 The EAC shall submit minutes of its formal meetings to the Executive Board, but need not prepare separate formal reports on its activities. Its Chairman shall brief the Executive Board on the work of the EAC at the conclusion of the annual audit.

3. Procedures

The EAC shall have access to information in possession of the IMF as needed to carry out its function, and will determine its own procedures to fulfill its responsibilities to the best of its professional ability. Members of the EAC undertake to protect the confidentiality of their service and the information obtained during the course of their duties.

It is expected that the EAC will meet at least twice a year. The members of the EAC shall be available for consultation on any emerging audit matters throughout the year. A preliminary two- to three-day visit shall take place in January in order for the EAC to review and discuss the audit plan with the external audit firm and IMF staff, and to get an update from the Treasurer's Department and the Office of Internal Audit and Inspection on recent developments within the IMF. Any newly appointed member of the EAC is expected to arrive a few days before returning committee members to be briefed on the IMF in general. No formal reports would be issued during this visit, but minutes of formal meetings would be sent to the Executive Board for information.

A second visit shall take place in June when the annual audit has been substantially completed by the external audit firm. At that time, the external audit firm shall submit its full audit report to the EAC for review. The EAC shall discuss the audit report with the external audit firm, the Treasurer's Department, the Office of Internal Audit and Inspection, and other departments, as necessary, with regard to substantive audit matters and the overall audit process. The EAC may decide to meet in

executive sessions with the external audit firm or staff of the Office of Internal Audit and Inspection. At the conclusion of the EAC's second visit to the IMF, the Chairman of the EAC shall give the Executive Board a briefing on the EAC's work. A formal report from the EAC to the Executive Board is not required.

4. Amendment to the Terms of Reference

In accordance with the provisions of Section 20(c) of the By-Laws, the EAC shall review its terms of reference periodically and may recommend amendments for consideration by the Executive Board.

Annex III. Comparison of Key Proposed Changes with Benchmarks

	Selected Best Practice Guides			Selected International Organizations						
	IIA ^{1/}	AICPA ^{2/}	UK ^{3/}	UNDP	ECB	WB	IADB	ADB	EIB	BIS
Purpose										
Full list of overseen areas in the purpose	v			v	v	v	v	v		v
Specific Responsibilities										
Financial and related reporting practices										
Review unusual transactions or changes in		v	v	v		v	v	v		
Assess adequacy of key accounting assertions and disclosures		v	v	v		v		v		
External audit framework										
Review independence of the external audit firm, approve		v	v		v	v	v	v	v	v
System of internal controls										
Include risk management in the audit committee scope	Include	Include	Include unless addressed separately	Does not include	Under internal controls	Include	Include	Include	Under internal controls	Under internal controls
Review systems to report ethics issues	v	v	v	v	v	v	v	v		
Internal audit framework										
Discuss internal audit adherence to the IIA	v	v	v		v	v	v			
Oversight of other audit-related issues										
Allow for other responsibilities	v	v		v	v		v			
Confidentiality and conflict of interest										
Provisions regarding members independence	v	v	v	v	v			v		
Work modalities										
Work procedures										
Provisions on voting	n/a – specific to Fund’s practices									
Work plan										
Develop work plan	v	v		v			v			
EAC effectiveness and training										
Review effectiveness	Annually	Annually	Annually	From time to time	At least every 3 years	Annually	Periodically	Annually	Not mentioned	Not mentioned
Reporting to the Board										
n/a – specific to Fund’s practices										

Annex IV. EAC Role and Responsibilities—History

The External Audit Committee was established in 1947. Under the original version of Section 20 of the Fund's By-Laws, adopted at the inaugural meeting of the Board of Governors, the Executive Board was given the responsibility for the audit of the financial statements. However, this role of the Executive Board was questioned at the first Annual Meeting of the Fund in 1946, and at the second Annual Meeting in 1947, an amendment of Section 20 of the By-Laws provided for the establishment of an external audit committee, separate and independent of the Executive Board.

Initially, the EAC was responsible for undertaking a comprehensive audit and reporting its view of the Fund's financial position. The EAC consisted of three members, who were typically independent accountants or auditors in public service: two serving one-year terms, and one for two consecutive terms to provide continuity. The Executive Board selected three member countries, which nominated candidates who in turn were confirmed by the Executive Board. The EAC submitted its audit reports on the Fund's financial statements to the Board of Governors through the Managing Director and the Executive Board. The audit opinion was signed by the EAC members, and the involvement of the Executive Board in the external audit function was minimal.

In 1978, an external audit firm started to assist the EAC in performing the audit. It was acknowledged that the accounts had become more complex and the Managing Director was authorized to engage an external audit firm to assist the audit committee in the performance of its functions. With this change, the audit firm conducted the audit procedures while the EAC continued to sign the audit report. The full EAC assembled in Washington for a three-week period each year after the external audit firm had substantially completed its audit. Prior to that, the continuing EAC member visited the Fund early in the calendar year to review the external audit plan. The audit firm followed detailed instructions from the EAC.

In 1999, the EAC was strengthened and its role and functions were clarified. An external consultant assisting with a review concluded that the external audit process should remain functionally independent of the Executive Board.⁸ The consultant did, however, recommend amendments to the EAC's role, which were implemented by the Fund: (i) the composition of the EAC was strengthened and the EAC would no longer be responsible for the certification of the Fund's financial statements on the basis of work conducted by an independent accounting firm; instead, the EAC would have general oversight of the annual audit; (ii) the annual audit, and issuance of an audit report, would be conducted by an external audit firm selected by the Executive Board in consultation with the EAC and appointed by the Managing Director; and (iii) as part of its oversight role of internal control, the EAC would review the adequate discharge by OIA of its responsibilities.

¹ *Review of the Fund's External Audit Function* (EBS/99/23, 3/1/1999).

Subsequent to 1999, several enhancements were introduced over the years to further strengthen the EAC oversight role.

- Up until 2005, the EAC spent on average six days per year onsite at the Fund. By 2016, the number of days spent onsite increased to average about 12 per year.
- Since 2006, the EAC expanded the number of departments with which the EAC meets during onsite visits and added a one-day visit in July.
- Since 2008, staff has organized informal sessions for EAC members to meet with three groups of Executive Directors during the planning and year-end visits.
- In 2013, staff reviewed certain aspects of the external audit arrangements.⁹ The review considered increasing the terms of service and/or number of the EAC members, but Directors broadly agreed that the three-member three-year arrangement remained appropriate. To further increase the effectiveness of new EAC members, the Board supported staff's proposal to lengthen and deepen the onboarding process for new EAC members.
- In 2014, the EAC was assigned additional oversight responsibilities with respect to the external audit firm independence.¹⁰ The new responsibilities include (i) providing an opinion at the time of the selection of a new external audit firm on whether its existing consulting contracts could compromise its independence and (ii) confirming to the Executive Board that the consulting services by the external audit firm contracted during a financial year did not compromise the independence of the external audit firm.
- In 2015, the July visit was extended to two days. This allowed the EAC to formally close out the annual audit process including conducting a lessons-learned session with staff, planning for the audit year ahead, and meeting with the incoming EAC member to ensure a smooth transition.
- In 2016, the Executive Board endorsed a new approach to mitigate conflicts of interest for EAC members by enhancing the selection process. The new measures also seek to ensure that EAC members remain independent throughout their tenure.

² *Aspects of the Fund's External Audit Arrangements—Issues Note* (SM/13/334, December 24, 2013).

³ *Proposed Modification of the Policy on Provision of Consulting Services by the External Audit Firm—Revised Proposed Decision* (EBAP/14/46, Supplement 1, 5/27/2014).