

The logo of the Asian Development Bank (ADB) consists of the letters 'ADB' in a white, serif font, centered within a dark blue square.

Asian Development Bank

Board of Directors
Audit Committee

Annual Report

Annual Report of the Audit Committee of the Board 2012–2013

August 2013

ABBREVIATIONS

ACB	–	Audit Committee of the Board
ADB	–	Asian Development Bank
BPMSD	–	Budget, Personnel and Management Systems Department
CTL	–	Controller's Department
FASB	–	Financial Accounting Standards Board
FY	–	fiscal year
ISTS-II	–	Information Systems and Technology Strategy II
ISTS-III	–	Information Systems and Technology Strategy III
IT	–	information technology
MAP	–	Management action plan
MD&A	–	Management's discussion and analysis
MDB	–	Multilateral development bank
OAG	–	Office of the Auditor General
OAI	–	Office of Anticorruption and Integrity
OAS	–	Office of Administrative Services
OCO	–	Office of Cofinancing Operations
OCR	–	Ordinary Capital Resources
OGC	–	Office of the General Counsel
OIST	–	Office of Information Systems and Technology
ORM	–	Office of Risk Management
OSEC	–	Office of The Secretary
OSFMD	–	Operations Services and Financial Management Department
PSOD	–	Private Sector Operations Department
S&P	–	Standard & Poor's
SRP	–	Staff Retirement Plan
TD	–	Treasury Department
U.S. GAAP	–	Generally Accepted Accounting Principles in the United States
VPFR	–	Vice President for Finance and Risk Management

CONTENTS

I.	INTRODUCTION: Composition of the Audit Committee of the Board and Meetings	1
II.	INTERNAL AUDIT	1
	A. OAG's 2012 Annual Report and 2013 Internal Audit Work Program.....	1
	B. OAG's Activity Reports	2
	C. External Auditor Performance for 2012 and Non-Audit Services.....	2
	D. Update on Selection of External Auditor (2014–2018)	2
III.	EXTERNAL AUDITOR.....	2
	A. External Auditor's 2012 Interim Update on the Statutory Audit and Attestation.....	2
	B. External Auditor's Report on the 2012 Audit of ADB	3
	C. Strategy Memorandum 2013 and Accomplishments in 2012	3
IV.	THE FINANCIAL STATEMENTS.....	3
V.	ANTICORRUPTION AND INTEGRITY: Quarterly Updates and Annual Report	4
VI.	INFORMATION TECHNOLOGY GOVERNANCE REVIEW AND IMPLEMENTATION	5
VII.	RISK MANAGEMENT OVERVIEW	5
VIII.	DISASTER PREPAREDNESS AND RESPONSE.....	6
IX.	AUDIT COMMITTEE WORK PROGRAM.....	7
X.	RECOMMENDATION TO THE BOARD.....	7

APPENDIXES

1.	Terms of Reference	8
2.	Work Program, 2012–2013	13

I. INTRODUCTION: COMPOSITION OF THE AUDIT COMMITTEE OF THE BOARD AND MEETINGS

1. This report covers the activities of the Audit Committee of the Board (ACB) from 1 July 2012 to 30 June 2013. The members of the ACB during this period were:

- (i) Executive Director Jérôme Destombes;
- (ii) Executive Director Robert M. Orr;
- (iii) Executive Director Ashok Lahiri (from November 2012, replacing Phil Bowen);
- (iv) Executive Director Gaudencio Hernandez, Jr.;
- (v) Alternate Executive Director M P D U K Mapa Pathirana (from April 2013, replacing Wilson Leonard F. Kamit); and
- (vi) Alternate Executive Director Dominic Walton-France (from February 2013, replacing C.J. Stan Vandersyp).

2. From 1 July 2012 to 30 June 2013, the ACB met 17 times and continued to operate under the terms of reference approved by the Board of Directors on 3 September 2010 (Appendix 1). In the course of these meetings, the ACB met with staff from the Controller's Department (CTL), the Office of the Auditor General (OAG), the Office of Anticorruption and Integrity (OAI), the Office of Information Systems and Technology (OIST), the Treasury Department, the Office of Risk Management (ORM), the Office of Administrative Services (OAS), the external auditor (Deloitte & Touche, Singapore), and other departments and offices of the Asian Development Bank (ADB). The work program is in Appendix 2.

II. INTERNAL AUDIT

3. The ACB reviewed the following reports:

- (i) OAG's 2012 Annual Report and 2013 Internal Audit Work Program;
- (ii) OAG's Activity Report as of 30 June and 31 December 2012;
- (iii) External Auditor Performance for Fiscal Year 2012—Summary of Survey; and
- (iv) OAG's Summary of Non-Audit Services provided by Member Firms of the External Auditor.

A. OAG's 2012 Annual Report and 2013 Internal Audit Work Program

4. The ACB reviewed OAG's 2012 Annual Report. The report contained audits and advisory services, including diagnostic reviews of several field offices, delivered by OAG in 2012. Other OAG activities performed during the year included external audit coordination, outreach activities, interagency collaboration, and continuous improvement processes. The report also contained an update on the implementation of external quality assurance recommendations. The OAG completed 26 audits in 2012; a further 11 audits were started that will conclude in 2013. The overall conclusion was that there was no material internal control weakness in processes reviewed.

5. The ACB also reviewed OAG's 2013 Internal Audit Work Program. ACB members were provided with an overview of OAG's risk assessment process to determine the annual work program. The process involved defining the audit universe and assigning risk ratings that considered previous OAG audits and discussions with management and the ACB. The ACB expressed its support of the work program, while noting that it might be ambitious and asked the new auditor general to revisit it. The new auditor general is aware of the ACB's concern and has

ensured that the work program will be managed by not taking on new assignments. During the period between the departure of the former auditor general on 31 October 2012 and the arrival of the new auditor general on 1 April 2013, the assistant auditor general served ably as the officer-in-charge.

B. OAG's Activity Reports

6. The ACB reviewed OAG's audit activity reports for the periods ending on 30 June and 31 December 2012. The reports included audit and advisory services completed during these periods; an inventory of audit recommendations resulting from high and medium risk findings; and an aging analysis of ongoing audit recommendations. Audit findings and recommendations on sovereign, nonsovereign transactions, information technology, the treasury, risk management, and finance and administration were discussed.

C. External Auditor Performance for 2012 and Non-Audit Services

7. As per the Board paper, Principles for Selection of Outside Auditor¹, the ACB shall review the external auditor's performance annually. On behalf of the ACB, OAG surveyed six business units (CTL, the Treasury Department, ORM, OIST, OCO, and BPMSD) on their assessment of the external auditor's performance for 2012. The results of the survey were presented to the ACB, which noted the performance of the external auditor to be above average.² OAG also reported on a quarterly basis, to the ACB the non-audit services provided by the external auditor.

D. Update on Selection of External Auditor (2014–2018)

8. The ACB was briefed on the progress of the selection of the external auditor for 2014–2018, which is expected to be completed by October 2013. A committee comprising members from CTL, OGC, OIST, OSFMD, and TD, chaired by the Vice-Presidency of Finance and Risk Management (VPFR), formed to evaluate the proposals for external audit firms. An ACB member was also appointed as an observer.

III. EXTERNAL AUDITOR

9. The ACB reviewed the following reports of the external auditor, Deloitte & Touche:

- (i) 2012 Interim Update on the Statutory Audit and Attestation;
- (ii) Report on the 2012 Audit of the Asian Development Bank; and
- (iii) 2013 Audit Service Plan and Accomplishments in 2012.

10. The ACB met with the external auditor, including in executive sessions.

A. External Auditor's 2012 Interim Update on the Statutory Audit and Attestation

11. The ACB discussed the status of the statutory audit and attestation conducted by the external auditor, as well as findings noted during the interim audit. The external auditor confirmed that no significant deficiency had been found during the audit of the 2012 Financial Statements.

¹ R138-10 dated 27 August 2010

² Based on an overall performance rating of 4.92 on a scale of 1 to 7, where 4 would be average.

B. External Auditor's Report on the 2012 Audit of ADB

12. The external auditor reported that the audit was completed and expressed its opinion that the financial statements prepared by ADB are presented fairly, in all material respects, and in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP). The external auditor confirmed its independence, noting that it was not aware of any relationships between Deloitte & Touche or its member firms and ADB, or of persons in financial reporting oversight roles at ADB, that might reasonably be thought to bear on Deloitte & Touche's independence.

13. The four audit work areas of primary focus were: (i) fair values of financial instruments; (ii) financial instruments classification; (iii) provision for allowance for loan losses; and (iv) the Staff Retirement Plan (SRP) and post-retirement medical benefits. Once again, the ACB noted the uncorrected misstatements relating to the accounting treatment for transfers of ordinary capital resources (OCR) income to Special Funds as an equity transaction (per ADB), and as an expense (per Deloitte).

C. Strategy Memorandum 2013 and Accomplishments in 2012

14. In accordance with ADB's regulation, the current engagement partner from Deloitte & Touche will need to be rotated after 5 years. The ACB met with the new engagement partner to enable continuity should Deloitte & Touche be appointed as the external auditor in 2014.

15. The ACB discussed the external auditor's audit strategy for 2013. The external auditor's areas of focus for 2013 were prepared based on management feedback and experience from last year's audit. In 2013, the external auditor will focus on four key risk areas: (i) loan impairment assessment; (ii) valuation of complex financial instruments; (iii) the valuation of the SRP liability; and (iv) accounting for equity investments, including recognition of equity income. The ACB agreed that, as in the past, the audit activities will include: (i) financial statements, comprising ADF and the special funds; (ii) trust funds administered by ADB; and (iii) a pension fund. The external auditors will also evaluate (i) the impact of new accounting standards effective as of 2013; and (ii) internal controls over financial reporting, including general information technology controls and components of key operating systems.

16. The external auditor stated that the audit strategy for 2013 may need to be recalibrated during the year and will be updated in November 2013.

IV. THE FINANCIAL STATEMENTS

17. The ACB reviewed the following reports:

- (i) quarterly financial statements for the periods ending 30 June 2012, 30 September 2012, and 31 March 2013; and
- (ii) ADB's annual financial statements as of 31 December 2012.

18. The ACB was apprised of issues and developments related to the financial statements. With regard to the issue mentioned in paragraph 13 above, the ACB shared its staff's opinion that per ADB's accounting the transfer of OCR net income could be treated as an equity transaction, while Deloitte considers that it should be accounted as an expense. However, Deloitte does not consider the amount involved to be material and so there is no impact on their opinion.

19. The ACB noted no significant deficiency or material weakness during the assertion and attestation process in 2012, and that ADB's internal controls over financial reporting remain effective.

20. The ACB was apprised of and extensively discussed the current level of unfunded liabilities in the SRP as reported in the 2012 year-end financial statements. The ACB initiated a memorandum signed by 12 Board members and issued on 12 April 2013 to the chair of the Pension Committee. The committee's concern about the financial sustainability of the SRP and its implication for ADB's lending activities was reflected in this memo. The ACB noted that one outcome of the memo has been agreement from Management to initiate a review of the SRP during the third quarter of 2013. The ACB will continue to review and discuss pension fund related matters that may affect the financial statements.

21. The ACB also discussed ADB's current position on the two financial reporting frameworks: International Financial Reporting Standards and U.S. GAAP. The members were assured that they would be informed of any significant developments (such as financial instruments classification and measurement or impairment) as needed.

22. A new standard requirement by the Financial Accounting Standards Board that affected the 2012 financial statements expands disclosure and adds quantitative information about unobservable inputs and their impacts on the fair value measurement of financial instruments.³ The ACB urged Deloitte to look at this issue as part of their 2012 year-end audit. The ACB was also briefed about two new updates by the Financial Accounting Standards Board, effective for 2013. These updates will expand the disclosures in the financial statements.

V. ANTICORRUPTION AND INTEGRITY: QUARTERLY UPDATES AND ANNUAL REPORT

23. In addition to the OAI annual report, there were four quarterly presentations made. The ACB was apprised of the approval of both (i) ADB's Integrity Principles and Guidelines, which incorporated harmonized corporate group guidelines, new provisions on temporary suspension, and voluntary disclosure and refinements to the provisions on cross debarment and sanctions violation for multilateral development banks (MDBs); and (ii) interdepartmental working groups to strengthen internal controls in anti-money laundering, as well as consideration of public sector due diligence.

24. OAI's briefings included those on (i) anticorruption week; (ii) project procurement related reviews (conducted jointly with regional departments that facilitate knowledge transfer of forensics audit skills) that were positively received by the recipient countries; (iii) training activities; (iv) various MDB (Heads of Integrity)/international financial institution meetings attended (including those with the U.S. Senate Foreign Relations Committee, and U.S. Treasury); (v) implementation of a due diligence mandate; (vi) implementation, with the involvement of resident missions, of the anticorruption day activities, and learning programs; (vii) new challenges relative to co-financing matters with certain bilateral and UN agencies (lack of a harmonized approach with bilateral and UN agencies as opposed to MDBs that have already harmonized their processes and definitions); (viii) recent developments at the World

³ "Unobservable inputs" are significant assumptions or inputs used in the valuation of financial instruments that are not observable in the market and that therefore necessitate the use of internal information, rather than information gathered from external sources. Unobservable inputs are based not on independent sources but on the reporting entity's own assumptions about the assumptions market participants would use.

Bank on sanctions reform (including the publication of the Bank's sanctions committee's decisions, and possible revision of the sanctions committee's composition to include only external parties); (ix) rolling out of an audit management system (for proper IT management system for project procurement related reviews); and (x) close coordination with the Budget, Personnel, and Management Systems Department to clarify administrative orders on the implementation of the whistleblower protection policy. OAI received 240 new complaints in 2012, and handled a total caseload of 449 investigations and complaints, while ADB issued 188 debarments of entities and individuals (inclusive of cross-debarments).

VI. INFORMATION TECHNOLOGY GOVERNANCE REVIEW AND IMPLEMENTATION

25. The ACB received updates on the IT organization's Management Action Plan (MAP) for governance reform and its present capacities as one element of OIST's transformation road map. In 2012, an independent high-level review of MAP implementation status was conducted as part of the Information Systems and Technology Strategy II (ISTS-II) completion review. Interviews were held with OIST and stakeholder staff. Likewise, reviews of IT policies, processes, and procedures were also conducted. The review was made by an external consultant over a six-week period, from October to November 2012.

26. MAP focus areas include IT risk management and sourcing and procurement, both of which exceeded target maturity levels. Significant improvements were seen in (i) IT governance; (ii) IT management; (iii) solution delivery; (iv) quality management; (v) talent management; and (vi) financial management. On the other hand, only marginal improvements were noted for (i) strategy and operational planning; (ii) IT service management; (iii) application management; and (iv) architecture management. No noticeable progress was found for (i) business-IT partnership; (ii) program and portfolio management; and (iii) infrastructure management. Only minimal improvement was expected from infrastructure management as initial maturity had already been assessed as high, while specific next steps were defined for both business-IT partnership and program and portfolio management.

27. OIST also reported on the early achievement of its 2012 target to close by year-end all due and overdue high-risk items identified by internal audit and independent verification and validation reviews over ISTS-II. This is the fourth straight year, since 2009, that OIST has achieved this.

VII. RISK MANAGEMENT OVERVIEW

28. Throughout the reporting period, the Office of Risk Management (ORM) presented key portfolio developments, explained their focus for risk issues, and presented updates on policies and methodologies. Updates on the implementation of the recommendations of PricewaterhouseCoopers, the previous external auditor, as well as staffing resources, were discussed throughout the year. The head of ORM provided quarterly updates on (i) overall sovereign portfolio quality and concentration; (ii) nonsovereign portfolio credit quality and equity valuation; (iii) quarterly assessment of expected loss and capital adequacy; and (iv) information on watch-listed and impaired transactions. Highlights of discussion included: (i) the continued rollout of the operational risk management framework across ADB; (ii) the annual assessment of equity investments, including the internal rate of return by investment type and an in-depth analysis of private equity funds; (iii) expected loss and provisioning; (iv) revision of the minimum planning equity-to-loan ratio; (v) use of "a probability of default weighted average risk rating" (more accurate in capturing the true risk of default in the portfolio compared to a simple weighted average risk rating); (vi) the reporting of heads of ORM and TD to the VPFR following

bank reorganization of vice presidencies; and (vii) the annual assessment of ADB's capital adequacy.

29. Members have shared their views and highlighted a few pressing issues to be discussed in more detail, including: (i) a projected level of nonsovereign share of operations of 13% by 2021 (and whether this is consistent with Strategy 2020's 50% new approval target); and (ii) the risk-bearing capacity of the balance sheet, specifically, accommodation of nonsovereign exposure, which carries a higher capital allocation.

30. In its discussion of a highlighted operational risk the ACB supported the need to review risk mitigation measures through a directors' and officers' liability insurance scheme for ADB-appointed directors in companies in which ADB has taken an equity investment. This insurance indemnifies the insured against damages, legal representation expenses, defense costs, and punitive damages brought against nominee directors. The ACB was informed that (i) ADB is currently self-insuring itself against any financial costs associated with defending the institution and its staff from potential liabilities arising as a result of staff acting as nominee directors; and (ii) only some companies in which nominee directors are appointed provide such insurance. The ACB noted that (i) there is a need to implement a more rigorous training program to educate staff and make them aware of their potential exposure to liabilities as nominee directors; (ii) a working group comprised of PSOD, OAS, ORM, OGC, BPMSD, and OSEC has been formed that will determine whether ADB should purchase insurance to protect ADB staff that are nominated as nominee directors. PSOD informed the ACB about a meeting hosted by its director general regarding the corporate governance framework among MDBs.

31. The ACB was also updated jointly by ORM and the Treasury Department on ADB's rating by Standard & Poor's (S&P) under its new rating criteria for multilateral lending institutions. It was noted that S&P has affirmed ADB's AAA rating. Members discussed at length the following two key steps in S&P's new rating criteria: (i) to assess ADB's standalone credit profile; and (ii) to assess the value of extraordinary shareholder support through callable capital. S&P's rating of the standalone credit profile involves assessments of ADB's policy importance, governance, management expertise, capital adequacy, funding, and liquidity. The final rating takes into account the value of extraordinary shareholder support, which is measured by the amount of ADB's callable capital from AAA-rated members. As of June 2013, S&P has given ADB a standalone credit profile of "aaa" and confirmed its AAA rating with stable outlook.

VIII. DISASTER PREPAREDNESS AND RESPONSE

32. OAS presented the ACB with an overview on the calamity risks for Metro Manila and highlighted several key findings, including ADB's lack of sufficient resources, personnel, and institutional authority to prepare for and cope adequately with a major disaster. ACB suggested that OAG consider an audit of disaster preparedness, and that OAS come up with two separate proposals on business continuity and staff welfare and wellbeing. A high priority would be to initiate obtaining technical assistance to develop a plan with alternatives. On 16 May 2013 the ACB in its memo to management shared its concerns on this matter. The ACB noted that a key risk in the event of a major earthquake would be the disruption of treasury or controller functions beyond 5 days, in which case ADB might encounter financial and reputational impacts such as default on bond payments. Management acknowledged this issue and promised to address it in due course. The ACB will continue to receive updates and seek management's views on the cost effectiveness of, and ability to implement necessary preparedness measures.

IX. AUDIT COMMITTEE WORK PROGRAM

33. For the next reporting period from 1 July 2013 to 30 June 2014, the ACB will also include the following activities in its work program:

- (i) select an external auditor for FY2014–2018;
- (ii) monitor the implications of the new S&P methodology for assessing the capital adequacy of multilateral lending institutions, and of any new rating issued by other rating agencies for ADB as well as other MDBs;
- (iii) monitor consideration of, and issues related to, the possible adoption of international financial reporting standards;
- (iv) update the implementation of the Management Action Plan on IT Reforms;
- (v) review operations and treasury risk management in ADB, including the risk implications of nonsovereign operations and of investments included in watch lists;
- (vi) monitor ADB's exposure to post-retirement benefits (pension and medical);
- (vii) review the progress following endorsement of the operational risk management framework by the Risk Committee, as well as the progress made by ADB in implementing the risk management framework presented to the ACB on 16 January 2012;
- (viii) review the business continuity management and disaster preparedness framework and action plan;
- (ix) review and follow up on non-audit work by the external auditor;
- (x) follow up on ADB's policy vis-à-vis tax havens and offshore financial centres, as well as the implementation of the recommendations made in the Second Review of Enhancing the ADB's Role in Combating Money Laundering and the Financing of Terrorism issued in November 2012.

X. RECOMMENDATION TO THE BOARD

34. The ACB recommends that this annual report be publicly disclosed after its consideration by the Board.

Audit Committee of the Board Terms of Reference

The Audit Committee of the Board of Directors was established pursuant to Section 12 of the By-Laws of the Asian Development Bank (ADB). Its function is to assist the Board of Directors in carrying out its responsibilities as they relate to matters such as ADB's financial reporting and audits, including internal controls and risk management, in line with Article 31 of the Agreement Establishing the Asian Development Bank.

1. AUTHORITY

1.1 In discharging its oversight functions over matters within the scope of its responsibilities, the Audit Committee of the Board is authorized to

- (i) perform activities within the scope of its terms of reference;
- (ii) seek any pertinent information from ADB, which shall not be unreasonably withheld;
- (iii) refer its requests for documents or information to the President;
- (iv) seek briefings on relevant auditing, accounting, risk management and internal controls, anticorruption and integrity, and financial matters it has identified from staff member(s) designated by the President, including such staff that the committee has suggested, and request their participation in meetings;
- (v) meet with the outside auditor, as necessary;
- (vi) advise the Board of Directors on the appointment of the outside auditor and consider any question of the outside auditor's resignation or dismissal; and
- (vii) consider the independence of the outside auditor, including the provision of non-audit services by the outside auditor to ADB.

2. COMPOSITION AND TENURE

2.1 The Audit Committee shall consist of no more than six members of the Board. The chair and other members shall be appointed by the President in consultation with the Board.

2.2 The committee members shall be free from any relationship that, in the opinion of the President, would interfere with the exercise of their independent judgment. The committee members shall inform the President of any circumstances that may reasonably be perceived to interfere with the exercise of their independent judgment.

2.3 The President shall, when appointing members of the committee, appoint at least one member with a background in accounting or related financial expertise who, through education and/or experience, would have a thorough understanding of financial, accounting, and auditing functions.¹ Members of the Audit Committee should have a working familiarity with basic

¹ Section 10(a) of the Rules of Procedures of the Board of Directors states: "Membership of the Committees established pursuant to Section 12 of the By-Laws need not be limited to Directors or their Alternates. The

finance, accounting, governance, internal audit, and risk management practices and principles and are strongly encouraged to enhance their familiarity with them by participating in educational programs. In circumstances where the committee requires specific advice and assistance to be able to perform its functions and such advice and assistance are not available, including from within ADB if appropriate, the committee may ask the President to engage such outside expertise and provide the necessary resources, which shall not be unreasonably withheld.

2.4 The committee shall be appointed for a term of 2 years, commencing 1 July each year in which the election of directors occurs. Members of the committee may be reappointed.

2.5 If a member of the committee ceases to be a member of the Board, the President, in consultation with the Board, shall appoint another Board member for the committee's remaining term.

3. MEETINGS

3.1 The committee shall meet as often as it considers necessary, but not less than once per quarter. Other Board members, as well as directors' advisors, may attend meetings of the committee as observers.²

3.2 The committee will meet with the outside auditor at least once a year without management or ADB staff present. In addition, the committee may meet with the outside auditor as and when considered necessary.

3.3 The quorum for meetings of the committee shall be three of its members. If the committee chair is unable to be present in person at a meeting, the members of the committee that are present shall select a member to preside.

4. RESPONSIBILITIES

The committee shall assess its work in its annual report and evaluate its performance annually relative to the committee's purpose and responsibilities outlined herein. The committee shall periodically review the adequacy of its terms of reference for possible adjustments as conditions dictate, and recommend necessary amendments to the Board of Directors for approval. The committee shall assist the Board of Directors in overseeing ADB's finances, accounting, internal control and risk management (including information technology systems and reputational risk), and anticorruption and integrity, and how these are being managed and accountabilities enforced. The committee shall satisfy itself that ADB's financial reporting and audits, including internal control and risk management, are adequate and efficient. In particular, the committee shall engage in the following:

A. Financial Reporting

4.1 Review and if necessary discuss with the controller the quarterly financial statements.

President, in consultation with the Board, shall appoint the members of committees and shall designate the chairmen thereof."

² Observers may participate in the deliberations at the invitation of the committee.

4.2 Review and discuss with the controller, auditor general, and outside auditor major accounting and auditing issues and financial statements, including any significant changes in the selection or application of accounting principles and auditing standards as well as the results of the audit by the outside auditor.

4.3 Review and discuss with the controller, auditor general, outside auditor, and other ADB staff as requested by the committee and/or designated by the President upon completion of the annual external audit and before the financial statements are published as well as the draft annual financial statements and related notes, the outside auditor's opinion, and the appropriateness of accounting principles, including disclosures through management's discussion and analysis (MD&A). Discussions will include management's assertion of internal controls over financial reporting and the outside auditor's attestation thereof. The committee will report on such discussions to the Board of Directors.

4.4 Meet with the controller and auditor general on a periodic basis to discuss any matters of concern regarding financial information and MD&A, internal control over financial reporting, and the assertion and attestation process.

4.5 Meet annually with the outside auditor to discuss management's assertions on the adequacy and appropriateness of internal control over financial reporting, and the outside auditor's attestation, including any significant deficiencies and/or material weaknesses in accordance with ADB's adopted attestation standard.

4.6 Meet with the general counsel to discuss any significant pending litigation that may have a material impact on ADB's financial condition. The committee will be informed on a timely basis of any such litigation.

B. Outside Audit

4.7 Appoint an observer to the Evaluation Committee for the selection of the outside auditor.

4.8 Review and discuss annually the outside auditor's scope of work and audit plan and any material changes to the audit plan during the year.

4.9 Review and discuss the outside auditor's performance and recommend to the Board of Directors for approval the appointment, reappointment for a contract period, or termination of the engagement of the outside auditor. Engagement or reappointment of the outside auditor will be in line with the Principles for the Selection of Outside Auditor.

4.10 Review and obtain a statement from the outside auditor to confirm annually the outside auditor's independence. Consider the provision of any other services by the outside auditor in accordance with the Principles for the Selection of Outside Auditor.

4.11 Review and discuss the outside auditor's annual report as a confidential document, and ensure that significant deficiencies and/or material weaknesses identified by the outside auditor, as well as other findings and recommendations made by the outside auditor and management's responses thereto, are reviewed, discussed, and appropriately acted upon. The committee shall review any recommendations and management's responses thereto, including their accompanying timetables, to address significant deficiencies and/or material weaknesses and to improve or establish necessary controls.

4.12 Meet separately, as necessary, with the outside auditor to review and discuss any matters that the committee or the outside auditor believe should be reviewed and discussed.

C. Internal Audit

4.13 Review and discuss annually the auditor general's scope of work and audit plan and any material changes to the audit plan during the year and, if necessary, request that specific audits be added to the work plan.

4.14 Review and discuss the effectiveness of the internal audit function.

4.15 Review and discuss, at least semiannually, an internal audit activity report, which should include a summary of recent audit reports and recommendations, the current inventory of outstanding audit recommendations, and the implementation progress of outstanding high risk audit recommendations. Ensure that significant internal audit findings and recommendations and management's responses thereto are considered. The committee will be informed of any significant audit findings on a timely basis.

4.16 Meet separately with the auditor general to review and discuss any matters that the committee or auditor general believes should be reviewed and discussed.

4.17 Be consulted prior to the engagement or appointment of, and on any intended removal of, the auditor general.

D. Risk Management and Internal Control

4.18 Review and discuss the efficiency, effectiveness, and integrity of the internal control system, including risk management; information technology security and control; and financial policies in such areas as trust fund administration, procurement policies and procedures, and financial management. Review and discuss pension fund related matters that may impact the financial statements.

4.19 Review and discuss with the controller, auditor general, head of the Office of Risk Management (ORM), chair of the risk committee, treasurer, and outside auditor, financial systems efficiency and the effectiveness of administrative procedures, and review internal control over financial reporting, including significant findings and recommendations and management's responses thereto.

4.20 Meet at least quarterly with the head of ORM to review and discuss the adequacy of ADB's risk management functions in order to ensure that appropriate risk management functions are in place.

4.21 Meet at least quarterly with the head of ORM to review and discuss assessments of ADB's risk exposure. The committee will be informed of any significant changes in assessments of ADB's risk exposure on a timely basis.

4.22 Receive prior advice on the engagement or appointment, and any intended removal of the head of ORM.

F. Anticorruption and Integrity Measures

4.23 Ensure that ADB has established and maintains appropriate, efficient, and consistent procedures for the receipt, retention, and treatment of complaints and anonymous submissions from internal and external complainants, including protection of “whistleblowers,” regarding fraud and corruption, or questionable accounting or auditing matters.

4.24 Meet at least quarterly with the Office of Anticorruption and Integrity (OAI) to discuss activities and outcomes of the anticorruption function, including cases where findings indicate systemic control weaknesses, or where they could constitute a reputational risk for ADB. The committee will be informed of any significant investigation findings on a timely basis.

4.25 Receive prior advice on the engagement or appointment, and any intended removal of the head of OAI.

G. Reporting Responsibilities

4.26 The committee shall

- (i) report annually on its activities and submit conclusions and/or recommendations to the Board of Directors, through the chair of the Board, who shall not unreasonably withhold them, as the committee deems appropriate;
- (ii) update the Board of Directors about the committee’s activities, as appropriate; and
- (iii) ensure that the Board of Directors is aware of matters that may significantly affect ADB’s financial affairs.

5. ADMINISTRATIVE ARRANGEMENTS

5.1 The channel of communication between the committee and ADB’s management and staff is through the secretary of ADB.

5.2 The Office of the Secretary shall be responsible for providing the necessary administrative services for the committee’s functioning, including providing a secretariat for the committee and maintaining its records.

**Audit Committee of the Board
Work Program, 2012–2013**

Dates of ACB meetings	Topics discussed
18 July 2012	Quarterly update from Office of Anticorruption and Integrity (30 June 2012) (OAI)
15 August 2012	Approval of Draft ACB Annual Report 2011–2012 (OSEC) Briefing on the MLI credit rating methodology (proposed by S&P) (ORM/TD)
29 August 2012	Audit Activity Report as of 30 June 2012 (OAG) Update on the implementation of the Management Action Plan on IT Reforms (OIST)
6 September 2012	Quarterly financial statements (period ending 30 June 2012) (CTL) Briefing on S&P's revised criteria for rating MLI after the joint consultation mission to S&P (ORM/TD)
2 October 2012	Risk management quarterly presentation as of 30 June 2012 (ORM)
16 October 2012	Quarterly update from the Office of Anticorruption and Integrity (30 September 2012) (OAI) Overview on the 2012 Assertion and Attestation Process (CTL)
29 November 2012	External auditor's update on Attestation and Statutory Audit (Deloitte)
7 December 2012	Quarterly financial statements (period ending 30 September 2012) (CTL) Debriefing on S&P's rating criteria for MLIs (ORM)
14 December 2012	Risk management quarterly presentation as of 30 September 2012 (ORM)
25 January 2013	Tentative work program for 2013 (OAG) OAI quarterly update (Q4 2012) Debriefing on ADB's rating by S&P under its new rating criteria (ORM/TD)
20 February 2013	OAI's 2012 Annual Report (OAI) OAG's 2012 Annual Report and 2013 Internal Audit Work Program (OAG) Disaster preparedness and response (OAS-SB)
7 March 2013	Working session on financial statements (CTL) 2012 Assertion and Attestation on internal control framework (CTL)
8 March 2013	Annual financial statements (Deloitte) Report on the 2012 Audit of ADB (Deloitte)
26 March 2013	Risk management quarterly presentation as of 31 December 2012 (ORM) OAG's Activity Report as of 31 December 2012 (OAG)
24 April 2013	Quarterly update from the Office of Anticorruption and Integrity (OAI) Update on the implementation of the Management Action Plan on IT Reforms (OIST) Others: Results of Deloitte's 2012 Performance (OAG)
4 June 2013	Quarterly financial statements (period ending 31 March 2013) (CTL) Discussion of ACB's Annual Report 2012–2013, and Work Plan 2013–2014 (OSEC)
25 June 2013	External auditor's Strategy Memorandum 2013 and Accomplishments in 2012 (Deloitte) Risk management quarterly presentation as of 31 March 2013) (ORM)

ACB = audit committee of the Board, ADB = Asian Development Bank, CTL = Controller's Department, IT = information technology, MLI = multilateral lending institution, OAG = Office of the Auditor General, OAI = Office of Anticorruption and Integrity, OAS-SB = Office of Administrative Services – Security, Business Continuity, and Government Relations Unit, OIST = Office of Information Systems and Technology, ORM = Office of Risk Management, OSEC = Office of The Secretary, S&P = Standard & Poor's, TD = Treasury Department.