



Financial Management of Donor Funds

Concessional Finance and Global Partnerships (CFP)

The World Bank





Contents

The World Bank's Role in Financial Management of Donor Funds / 1

Financial Management in Practice / 3

Extensive experience in managing donor assets / 3

Financial management of donor funds / 4

Investment management of donor funds / 6

Intermediation services in the capital markets / 8

Risk monitoring and control frameworks / 9

Regular financial reporting and independent audits / 11

Provision of financial and information systems / 11

Quality assurance and compliance monitoring / 12

Independent evaluation of projects and programs / 12

Oversight through the World Bank Board and committees / 12

Governance and Anti Corruption (GAC) agenda / 12

Disclosure and access to information / 13

Introduction

Many donor governments and organizations ask the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA), more commonly referred to as the World Bank, to manage funds originating from budgetary appropriations and other sources for economic and social development. This booklet describes how the World Bank manages these assets.

Since the creation of IDA in 1960, the World Bank's funding arm for the poorest, the number of contributors to IDA and trust funds has increased to about 245 different donors, including sovereign governments, foundations, non-governmental organizations and private donors. In fiscal year 2010 alone, these donors will provide an estimated \$20 billion of cash contributions to foster economic development and poverty reduction in low and middle-income countries. At end-March 2010, the World Bank managed a total of \$43.1 billion of liquid assets held by IDA and Trust Funds that will be disbursed across a wide range of sectors.

The World Bank uses financial management techniques to ensure that the funds provided by its donor partners are prudently managed. The growth of donor-funded development initiatives over the past decade is a testament to the confidence that donors place in the World Bank's adherence to high fiduciary standards of financial management.

Donor funds are managed through a number of financial services, ranging from standard banking services to investment management, currency risk management, and financial reporting. In managing these funds, the World Bank maintains secure information technology systems and adheres to a comprehensive internal control framework as well as internal and external audit reviews to provide assurance to donors that disbursements follow relevant World Bank policies and procedures for the funds it is entrusted with.

Sound financial management of donor contributions is a necessary and integral part of the value process to ensure the appropriate use of taxpayers' and other resources provided for the purposes of economic and social development. We look forward to working with donor partners to achieve sustainable outcomes in developing countries and economies in transition.

Axel van Trotsenburg
Vice President
Concessional Finance and Global Partnerships (CFP)
The World Bank



The World Bank's Role in Financial Management of Donor Funds

When donors provide funding to the World Bank to finance development projects and programs, they expect these funds to be well managed until they are disbursed. In short, financial management by the World Bank covers the process of sourcing funding from donors, investing the financial assets received, and disbursing funds to recipients. Within this value chain, the World Bank performs a variety of financial and risk management activities and services, including financial reporting, performing business processes and maintaining the requisite systems and control framework.

Within the World Bank, the Concessional Finance and Global Partnerships Vice Presidency (CFPVP) is responsible for resource mobilization and donor relations, policy development and advisory services, as well as financial and risk management for the International Development Association (IDA), Financial Intermediary Funds (FIFs), and Bank-executed and Recipient-executed trust funds.

Other units in the World Bank are also involved in the financial management of donor funds. These include the Legal Department, Controllers, Treasury, Corporate Finance, Information Technology, among others. Appraising and supervising World Bank-financed development projects is the responsibility of regional, sector and other vice presidencies.

World Bank Financial Management at a Glance

- Extensive experience in managing donor assets
- Financial management of donor funds
- Investment management of donor funds
- Intermediation services in the capital markets
- Risk monitoring and control frameworks
- Regular financial reporting and independent audits
- Provision of financial and information systems
- Quality assurance and compliance monitoring
- Independent evaluation of projects and programs
- Oversight through the World Bank Board and committees
- Governance and Anti Corruption (GAC) agenda
- Disclosure and access to information



Financial Management in Practice

Extensive experience in managing donor assets

The World Bank has mobilized and managed donor funding since 1960 when IDA was created to support the poorest countries through interest-free and long-maturity loans. Donor contributions are the main source of funding for IDA, complemented by credit reflows and contributions from World Bank net income and more recently grants from the International Finance Corporation (IFC). There are 45 donor governments contributing to the current IDA15 replenishment, including many middle-income countries and former IDA recipients. At the end of fiscal year 2009, the World Bank's Treasury managed some \$21.3 billion of cash and investments for IDA.

Since the 1980s, donors have also provided bilateral aid resources and other contributions through trust funds held by the World Bank, many of which are intended to co-finance World Bank-financed development projects. A trust fund is typically a financing arrangement set up with contributions from one or more donors. World Bank administered trust funds consist of Bank-executed trust

funds where the World Bank has spending authority and Recipient-executed trust funds where the World Bank passes funds on to a third party recipient while performing an operational (appraisal and supervision) role. Over the last decade donors have also engaged the World Bank for the management of another line of donor-funded development operations through Financial Intermediary Funds (FIFs), where the World Bank takes on a wide range of financial management and advisory roles while project implementation is carried out by other agencies or entities. A total of 245 donors from 77 countries are now supporting trust funds (including FIFs) financially, through 1,045 trust fund accounts, for which the World Bank held some \$19.9 billion of invested liquidity at the end of fiscal year 2009.

To manage these substantial donor financial resources, the World Bank follows prudent financial policies and procedures. It employs appropriate operational policies and compliance with established business procedures for appraising and supervising projects and an operational fiduciary framework including safeguards, project procurement and financial man-

agement for the recipients of the funds. Backed by its AAA credit rating, IBRD, the World Bank's arm that supports middle-income and credit-worthy low-income countries, acts as a trusted financial intermediary for IDA and Trust Funds in the international capital markets. Trust funds and IDA assets are kept separately and are not co-mingled with those of IBRD.

Financial management of donor funds

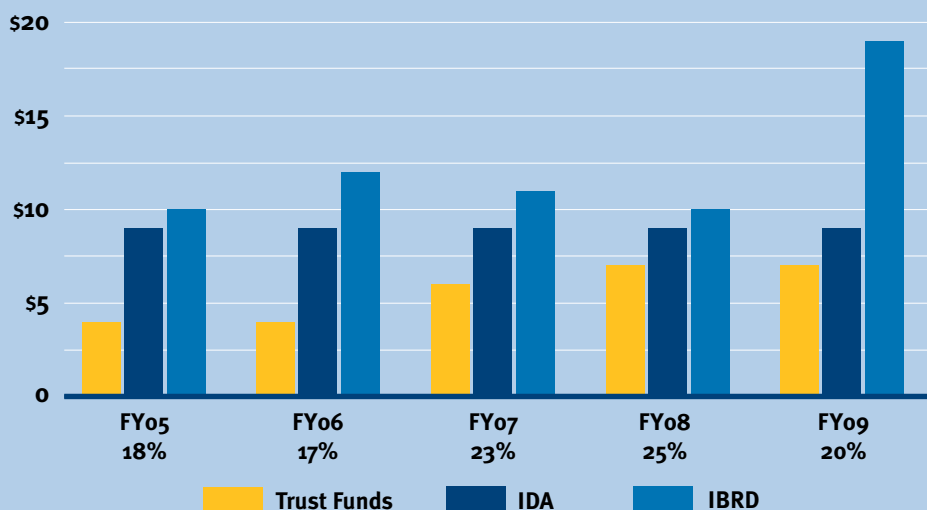
Financial management of donor funds starts by guiding donors through the process of making a contribution to IDA or a trust fund. This includes preparing the required legal documents and donor contribution agreements. Thereafter, the World Bank collects and manages the funds from donors, beginning with the process of sending

invoices to donors for their installment payments, followed by the processing of cash and promissory note payments received.

Financial management also extends to the recipient side of donor funded operations. The World Bank prepares and enters into grant and project agreements with developing countries and other recipients benefiting from the donor-provided resources. For financial intermediary funds project implementation is carried out by other agencies or entities. The fund balance is tracked to ensure that grant commitments for projects do not exceed available and expected funding. Forecasts are prepared to project the ability of a fund to commit grant amounts for future project disbursements. Cash flows and liquidity are managed in order to ensure that funds are available when required for

World Bank Disbursements, Fiscal Years 2005-2009

In US\$bn



WBG TF disbursements as percentage of total IBRD, IDA and TF disbursements



disbursement. Disbursements to the recipient are dependent on receipt of funds from the donors.

Allocations of funds for specific grants are recorded and tracked by the task manager of a trust fund. These allocations can encompass grant or loan commitments, administrative budgets, fees for project supervision, and other commitments. Commitments will translate into subsequent disbursements for eligible expenditures and transfers of funds to recipients.

Investment management of donor funds

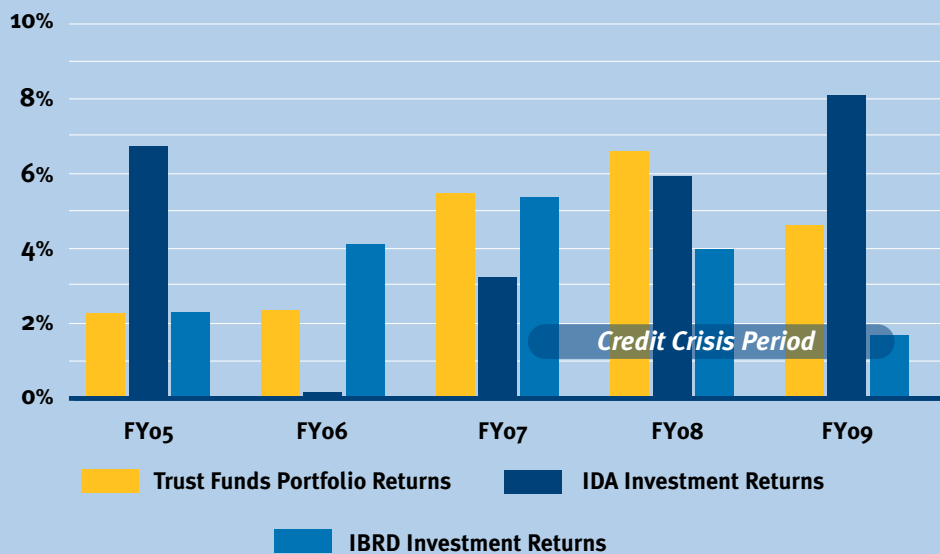
Between the receipt of funds from donors and their disbursement to grant recipients, the World Bank's Treasury invests the liquid assets in the capital markets. This is carried out prudently with

the primary objective of preserving the capital of the funds held.

The investment process starts by establishing an asset management strategy. Once this strategy is reviewed and approved by appropriate departments and financial committees, the World Bank's Treasury develops a strategic asset allocation to achieve the investment objectives. Suitable portfolio benchmarks are set to achieve the investment objectives and performance is closely monitored. Investment positions are established with approved market counterparties based on investment guidelines for which credit exposure limits are established and monitored continuously.

Trust funds assets are invested in three tranches with different risk and return profiles. All trust funds are reviewed with respect to their alloca-

Portfolio Investment Returns, Fiscal Years 2005-2009





Asset Management During the Global Financial Crisis

The World Bank took several steps to further safeguard donor assets and preserve their investment performance during the global financial crisis of 2008-2009. These included but were not limited to:

- Reducing the exposure of the portfolio to assets backed by residential home loans.
- Reducing the duration of the portfolio to limit sensitivity to widening credit spreads.
- Reducing exposure to financial institutions most adversely affected by the crisis.
- Regularly reviewing the portfolio to ensure adherence to credit rating constraints, as many institutions experienced credit rating downgrades.
- Limiting trading to the strongest counterparties to minimize risk due to counterparty failure.
- Strengthening collateral policies and procedures to reduce counterparty exposure.

tion into the different investment tranches, based on multi-year cash flow projections for each fund and risk/return considerations. For IDA, the investment framework is based on three liquidity tranches with different investment objectives, investment horizons and risk tolerances which are reviewed annually. Investment returns for trust funds and IDA are analyzed monthly and there are regular discussions to assess investment policy and asset allocations.

Intermediation services in the capital markets

IDA and Trust Funds are exposed to market risks due to movements in currency and interest rates, affecting the value of assets held in trust. Market risks are identified and hedging and other alternatives to mitigate these risks are approved by appropriate departments and finance committees. In the case of trust funds, where relevant, the Bank consults external governing bodies and seeks their approvals. Thereafter, the World Bank Treasury arranges the intermediation of market

transactions. One example is the contracting of currency hedges to manage a mismatch between the currency of donor contributions and the commitment currency of loans or grants for IDA.

The World Bank also provides customized financial services. One example is the design and evaluation of a market borrowing strategy, with subsequent execution services for bond issues of a given fund, such as the International Financing Facility for Immunization. In another example, on behalf of Carbon Fund participants, the World Bank enters into Emission Reduction Purchase Agreements (ERPAs). The World Bank also executes the monetization of the Carbon Emission Reductions (CERs) received on behalf of a fund; the monetization program converts CERs into cash to support commitments and disbursements to the funds' projects. For the poorest countries affected by droughts, the World Bank intermediates the purchase of drought insurance in the capital markets, with donors financing the resulting insurance premia. Other customized financial intermediation services can be provided as required by donors.



Risk monitoring and control frameworks

The World Bank monitors and reports on risk at the institutional and fund level. It uses an integrated risk management framework, providing a continuous, proactive and systematic process to analyze, manage and communicate risks from an institutional perspective to its Board and management. This includes regular risk scans, risk workshops and the World Bank-wide Risk Report that draws from institutional risk assessments and reviews performed by the World Bank's Internal Audit, Independent Evaluation and institutional Integrity units.

At the fund level, risk assessments are performed throughout the life of the fund by its assigned task managers, providing important input into the oversight and monitoring of funds. A separate Risk Report is prepared by CFP as part of its fiduciary oversight and financial management responsibility for IDA and Trust Funds. The report provides an assessment of risks in each

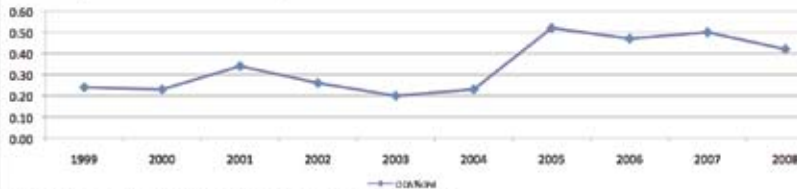
fund and program based on a customized set of risk metrics and serves as an input into World Bank-wide risk reports.

The World Bank mitigates financial and operational risks through strong internal controls and processes to safeguard donor assets. Controls are evaluated using the Committee of Sponsoring Organizations of the Treadway Commission (COSO), an internationally recognized and widely accepted internal control framework. The World Bank has in place a program to assess all of its business units and takes steps to strengthen and streamline its controls and business processes. Most recently, CFP carried out a Financial Management Review to ensure that financial transaction processing adheres to high operational standards and is sufficiently segregated, with effective controls and independent oversight. The World Bank is committed to continuously strengthen monitoring, oversight and controls for its donor-funded operations.

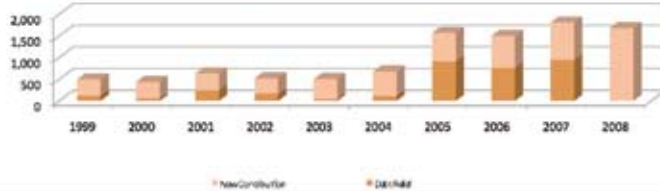
Donor Country: OECD/DAC Data

Source: OECD/DAC Database by Calendar Year (as of 05/06/2009) unless noted. Data not yet available for 2008 are shown as 0.

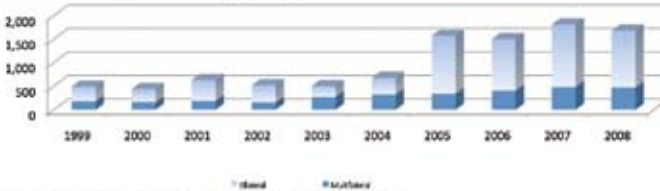
Donor Country - Total Net ODA as a Percentage of GNI



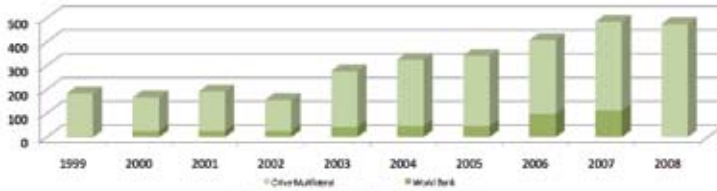
Donor Country - Total ODA: Debt Relief and New Contributions (in US\$M)



Donor Country - Total ODA: Multilateral and Bilateral (in US\$M)



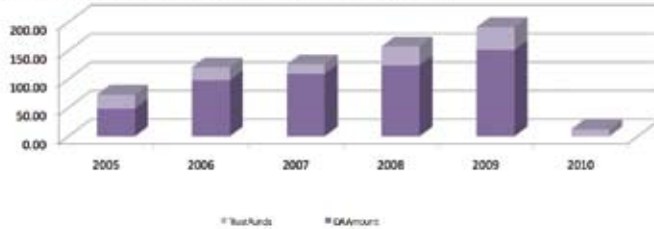
Donor Country - Multilateral ODA: World Bank and Other Multilaterals (in US\$M)



Donor Country - World Bank Data

Source: World Bank Contributions Paid-In (Cash + Notes) by Fiscal Year - data as of 11/13/2009 unless noted

Donor Country - Contributions Paid-In to the World Bank: IDA and Trust Funds (in US\$M)



Information Systems for Donors

Donor Center/Client Connections. Provides each donor and agency with up-to-date financial information on Trust Funds through a secure website (<http://clientconnection.worldbank.org>):

- Financial information updated daily
- Donor contributions for each trust fund and across the portfolio
- Disbursements for each trust fund by country and expense category
- Access to donor administration agreements
- Progress reports, completion reports and audit reports
- User access is managed by donor agency

AidFlows. Provides information on sources of donor aid contributions as reported by OECD and the World Bank. Information is available for 58 donor countries (www.worldbank.org/cfp, Financial Management, Donor Aid Contributions):

- Official Development Aid (ODA) as a percentage of GNI
- Contributions to the World Bank and other multilateral banks
- Contributions to IDA and World Bank-administered trust funds

A second phase of AidFlows is under development to provide information on the uses of funds by recipient country.

Regular financial reporting and independent audits

Financial transactions are accounted for and recorded using appropriate accounting systems. The World Bank ensures proper and secure maintenance of all accounting documents and records for IDA and Trust Funds.

Donors are provided periodic financial reports through the World Bank's Client Connection website (<http://clientconnection.worldbank.org>). At the end of each fiscal year, donors receive a Single Audit Report for all modified cash-basis trust funds, comprising (i) a management assertion together with an attestation signed by external auditors regarding effectiveness of internal controls over financial reporting of the modified cash-basis trust funds and (ii) a combined financial statement along with the external auditor's report. The World Bank arranges for separate external audits of financial statements for selected large trust funds where requested and separately funded by donors. For IDA, shareholders receive quarterly financial reports and annual audited financial statements, as well as a detailed Management Discussion and Analysis.

The internal audit function at the World Bank reports to the President of the institution. There are regular internal audits of IDA and Trust Funds, covering their business processes and the responsible units. Internal audits serve as an independent, third-party assessment of existing systems for risk management, the control framework, and governance processes.

Provision of financial and information systems

The World Bank uses integrated information systems that provide end-to-end financial transaction processing. Transactions include the recording of replenishment and contribution agreements, calls of resources from donors, foreign exchange, allocation of investment income, disbursement of funds, and associated reporting to donors in accordance with underlying agreements. The information technology systems provide donors as well as the implementing agencies and secretariats with data and customized reporting, as part of the World Bank's fiduciary responsibilities.

Most of the donor funding received for IDA and Trust Funds is processed through the System for Tracking and Accounting for Resources (STAR). STAR is a customized, flexible interface that lowers transaction costs, enhances business controls and reduces operational and financial risk. STAR provides a robust information technology platform for supporting an increasing number of complex and often customized donor-funded initiatives. It automates most financial functions and client relationship management. Since it is fully integrated, transactions in STAR are seamlessly transferred to the SAP general ledger.

STAR is used for donor contributions to IDA and Trust Funds as well as World Bank member subscriptions to IBRD, the Multilateral Investment Guarantee Agency, and the International Centre for the Settlement of Investment Disputes. The

World Bank is making significant investments in information security, and the governance and security of its information technology systems undergo continuous strengthening.

Donors have access to several system applications offering financial information on their contributions to IDA and Trust Funds. Two web-based applications are the Donor Center within the World Bank's Client Connection website and the AidFlows application (see Box for more details).

Quality assurance and compliance monitoring

The World Bank provides results measurement and quality assurance for IDA and trust fund operations through dedicated teams and units. Monitoring of compliance with applicable World Bank policies and procedures is in place, including periodic compliance testing of financial transactions for trust funds. For IDA, an extensive internal controls review has been undertaken over the past years, including a compliance component as part of that review. Compliance is part of the overall control framework used to provide donors with assurance that World Bank policies and procedures are being followed.

Independent evaluation of projects and programs

Regular evaluations are performed for World Bank-financed development projects as well as recipient-executed trust fund projects and programs. The Independent Evaluation Group is not part of Bank

management and reports directly to the Executive Directors of the World Bank. Evaluations aim to learn from experience and to offer an objective basis for assessing outcomes and results of development projects and programs. Lessons learned drawn from evaluations are disseminated publicly.

Oversight through the World Bank Board and committees

Institutional oversight over donor-funded programs is provided by the World Bank's Executive Directors, Committees of the Board, the President of the institution, as well as members of the senior management team. The highest management group to oversee the financial management for IDA and Trust Funds is the Finance Committee, chaired by the World Bank Group Chief Financial Officer. Subcommittees looking after new financial initiatives as well as financial strategy, risk management and performance complement this group.

A number of larger trust funds have separate external governing bodies and associated committees. The World Bank may serve as a member or observer with these governing bodies, in various capacities, and provide periodic trustee and financial reporting to them.

Governance and Anti Corruption (GAC) agenda

The World Bank has continuously stepped up efforts to strengthen governance and financial oversight in its partner countries where development projects are being implemented. The



World Bank's Governance and Anti-Corruption agenda is a core pillar in these efforts. It features capacity-building measures in member countries for combating corruption as well as measures to protect and enhance the integrity of the World Bank's operations.

The World Bank's Integrity Vice Presidency plays a central role in the fight against corruption. It investigates allegations of fraud and corruption as well as allegations of possible staff misconduct. It provides World Bank staff and clients with guidance for building preventive measures within development projects, including customized advice and training. A Fraud and Corruption Awareness Handbook helps staff and client counterparts identify possible fraud and corrup-

tion schemes that may become apparent during project design or implementation.

Disclosure and access to information

The World Bank is taking continuous steps to widen access to information and further enhance transparency. A new Access to Information Policy, effective July 1, 2010 provides a fundamental shift in the Bank's approach to disclosure of information, moving to an approach of general disclosure of information in its possession unless listed on a limited set of exceptions. The new policy provides access to more data than ever before, including information on projects under preparation or implementation as well as proceedings of the Executive Directors.

Financial Management of Donor Funds

The Global Fund to Fight AIDS, Tuberculosis and Malaria. The Global Fund to Fight AIDS, Tuberculosis and Malaria was established in 2002 to make a sustainable contribution to the reduction of infections, illness and death caused by three communicable diseases: HIV/AIDS, Tuberculosis and Malaria. Since the inception of the Global Fund, the World Bank has been working with the organization as a development partner in fighting these diseases, and as Trustee for the Global Fund Trust Fund. The World Bank is engaged in a trustee role whereby grant commitments and disbursements are executed upon instruction from the Global Fund Secretariat.

The Adaptation Fund. The Adaptation Fund is designed to finance climate change adaptation projects and programs that are country-driven and based on needs, views and priorities of eligible developing country Parties to the Kyoto Protocol. The Global Environment Facility Secretariat provides secretariat services to the Adaptation Fund and the World Bank serves as Trustee. In this role, the World Bank performs two core functions: (i) trust fund management; and (ii) monetization of Certified Emissions Reductions for the Adaptation Fund.

Financial management provided by the World Bank for the Global Fund and Adaptation Fund includes the following services:

- Formulation and negotiation of legal agreements with donors
- Management of the donor contribution process
- Investment management of cash contributions to the trust funds, including currency conversion
- Commitment and disbursement of funds
- Maintenance of accounting records of transactions and provision of appropriate reports
- Provision of the necessary information technology infrastructure



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