Assessing Risks Associated with Funding Development Initiatives Through Host Country Systems:

The USAID Public Financial Management Risk Assessment Framework (PFMRAF) and the Case of Honduras

David Colvin
President and CEO, IBI International

- Ownership
- Alignment
- Harmonisation
- Managing for Results
- Mutual Accountability
Objective 1: Strengthen partner country capacity to improve aid effectiveness and sustainability
Aim is to avoid creating parallel service delivery structures and instead focus on improving those that exist.
Direct funding conditional on PFMRAF (see ADS 220)
PFMRAF

- **Stage 1**: Rapid Appraisal (country level)
- **Stage 2**: Risk Assessment (institution level), Analysis, Mitigation, and the Approval for Use of Partner Country Systems
- **Stage 3**: Project Design, Approval, Designation of Responsibilities and Selection of the Funding Mechanism
- **Stage 4**: Negotiating and Preparing the Bilateral Project Agreement with the Partner Country Government
- **Stage 5**: Implementation, Monitoring, and Evaluation
PFMRAF (cont’d)

Current Status (as of Oct. 2013):

- 36 Stage 1 country-level assessments completed.
- 80 Stage 2 institution-level assessments at some stage of activity
USAID OVERSEAS MISSION FUNDING TO LOCAL GOVERNMENTS/INSTITUTIONS

Source: USAID Forward Progress Report 2013 and USAID Website Data Tables
Stage 2 Risk Assessments

Objective: identify fiduciary risks at the institutional level and develop mitigation measures

Usually done with a program design already in mind.

Positive Outcome = Approval of Use of Partner Country Systems
Stage 2 Case Study: MCA-Honduras

Context:

- Unique situation of an institution already set up for purpose of receiving, programming, accounting for USG funds. MCC Compact was for $215m.
- CABEI and IADB also using MCA-H as implementing agency.
- Total funding from inception through 2012 was $389m.
- PEFA report on overall PFM system completed in early 2013.
Risk Assessment

- IBI approach extended well beyond the application of the PFMRAF questionnaire to encompass a validation of the 2013 PEFA Report on the GoH PFM, and a capacity assessment of the MCA-H.
- Work performed included extensive testing of governance, control environment, transaction cycles, internal control, procurement and operational procedures of the MCA-H.
- Key point: institutions can’t be assessed in isolation. They exist within a system.
Analysis of six dimensions related to GoH PFM environment:

1. Budget Credibility
2. Budget Comprehensiveness and Transparency
3. Policy-Based Budgeting
4. Predictability and Control in Budget Execution
5. Accounting, Recording and Reporting
6. External Scrutiny and Audit
Analysis of 10 components related specifically to MCA-H

1. Governance, control environment, and organizational structure
2. Budgetary Systems
3. Budget Execution
4. External/Internal Audit Function
5. Internal Controls
6. Procurement
7. Human Resources
8. Revenues, Accounts Payable, and Expenses
9. Information Technology
10. Donor Relations
Risk Assessment

<table>
<thead>
<tr>
<th>Component</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Credibility of the budget</td>
</tr>
<tr>
<td>2 Comprehensiveness and transparency</td>
</tr>
<tr>
<td>3 Policy-based budgeting</td>
</tr>
<tr>
<td>4 Predictability and control in execution</td>
</tr>
<tr>
<td>5 Accounting, recording, reporting</td>
</tr>
<tr>
<td>6 External scrutiny and auditing</td>
</tr>
<tr>
<td>7 Governance, control env., structure</td>
</tr>
<tr>
<td>8 Budgetary systems</td>
</tr>
<tr>
<td>9 Budget execution</td>
</tr>
<tr>
<td>10 External/internal audit</td>
</tr>
<tr>
<td>11 Internal controls</td>
</tr>
<tr>
<td>12 Procurement</td>
</tr>
<tr>
<td>13 Human resources</td>
</tr>
<tr>
<td>14 Revenues, A/P, and expenses</td>
</tr>
<tr>
<td>15 Information technology</td>
</tr>
<tr>
<td>16 Donor relations</td>
</tr>
</tbody>
</table>

Impact Scale

GoH

MCA-H

GoH/MCA-H

Likelihood Scale

IBI International
Global Insights—Local Solutions
Illustrative Findings Matrix
Assessment Results

- Included an assessment of the MCA-H “residual risk” - i.e. risk remaining after mitigation measures are in place — e.g. audited semiannual progress reports, annual or project-end financial audits, etc.

- Our conclusion is that MCA-H relatively strong capacity effectively reduces risks posed by the larger PFM system in which MCA-H operates to a resultant level of risk ranging from medium to low.
Discussion Topics

• Is the MCA-Honduras a genuine host country institution, or is it a “parallel service delivery structure?”

• If this model succeeds in Honduras, should USAID seek to replicate the approach in other MCC countries?