A Risk-Based Approach to International Development

USAID and the Public Financial Management Risk Assessment Framework (PFMRAF)

Jason Wynnycky
Financial Management Policy Advisor
United States Agency for International Development
We partner to end extreme poverty and promote resilient, democratic societies while advancing our security and prosperity.
Why We Manage Risk?

AS REQUESTED, I DID A "RISK MANAGEMENT" ASSESSMENT.

I CONCLUDED THAT THERE WAS NO RISK OF ANY MANAGEMENT.

DO YOU HAVE ANYTHING TO ADD?

I'LL GET BACK TO YOU.
Definition of risk varies depending on the context and framework

- An **uncertain** event or condition that, if it occurs, has a positive or negative effect on a project’s objectives
- A **future uncertainty** that threatens the success of achieving program goals and objectives within defined cost, schedule and performance constraints
- **Potential** for an unwanted outcome resulting from an incident, event, or occurrence, as determined by its **likelihood** and the associated consequences
- Risk is the combination of the **probability** of an event with its consequences

All risks have a level of uncertainty in these definitions
Risk Management

A systematic process to identify and measure risks and determine appropriate actions for handling the risks

• Provides a framework for managing any form of risk in a transparent, systematic manner

• Helps policymakers assess risks, strategically align finite resources and take actions under conditions of uncertainty

• A process whereby organizations methodically address the risks attached to their activities to achieve sustained benefit
Why Risk Management?

Objectives

• Create value by aligning risk appetite and strategy to risk and return
• Minimize operational surprises and increase preparedness for crisis
• Ensure compliance with regulatory and statutory requirements
• Change the likelihood and consequences of risks
• Improve perception of the organization
• Increase stakeholder support

Benefits

• Improved decision making capability
• Stronger cost controls
• Increased efficiency and effectiveness in resource allocation
• Safeguard and enhance assets
• Greater probability of success and insight into preventive areas
A risk-based methodology for assessing a partner government’s public financial management (PFM) and accountability systems.

Designed to primarily identify and rate fiduciary risks and associated mitigation strategies based on project objectives and implementation mechanisms.

The PFMRAF is not a certification or seal of approval. It is an assessment of partner government systems and should be approached by the Mission and respective government as a partnership.

A management tool used primarily used to inform government-to-government (G2G) modalities in project design.

**PFMRAF: A two-stage, sequential process:**

**Stage 1 Rapid Appraisal** – a country level examination of the partner government PFM environment and associated fiduciary and related risks, as well as elements of governance and public accountability.

**Stage 2 Risk Assessment** – designed to identify, evaluate, and propose measures to mitigate transactional level risks of target partner government institution’s PFM systems at the country, sector, or sub-national government.
Civil service, human resources selection and retention, professional education, popular numeracy, professional qualifications, information/communications/technology capacity, financial sector capacity, auditing and accounting standards, internal control standards, internal audit operations

Media freedom, public sector behavioral standards (e.g. financial disclosure, conflict of interest, ethics) private sector behavioral standards (e.g. full disclosure, anti-trust, open competition, anti-fraud) CSOs and media watchdog, anti-corruption provisions, market-based deficit finance
Standard Risk Management vis-à-vis PFMRAF Methodology

Continuous Communication and Collaboration

**Plan Risk Management**
- Develop Risk Management Policy and Plan
- Conduct Interviews
- Review Systems
- [ex: PFMRAF]

**Identify Risks**
- Execute plan
- Identify Risks
- Develop Risk Register
- [ex: Stage 1 and 2]

**Analyze Risks**
- Qualitative and Quantitative Analysis
- Prioritize Risks
- Update Register
- [ex: Stage 2]

**Plan Risk Responses**
- Mitigation Strategies
- Contingencies
- Update Register
- [ex: Stage 2, Risk Mitigation Plan]

**Monitor and Review**
- Track Risks
- Implement Responses
- Update Register
- Evaluate Effectiveness
- Request Changes
- [ex: Risk Mitigation Plan, post-Stage 2]

**Continuous Communication and Collaboration**
PFMRAF in Perspective: The Program Cycle

- **AUPGS** – Approval for Use of Partner Government Systems
- **CDCS** – Country Development Cooperation Strategy
- **DOAG** – Development Objective Assistance Agreement
- **PAD** – Project Appraisal Document
- **PA** – Project Authorization
Risk Mitigation vis-à-vis Capacity Development

Focus on the envisioned G2G project

Risk Mitigation

Capacity Development

Focus on sustainable change and impact over time

Short and medium term actions to remediate risks primarily applicable to the respective project

Develop open and collaborative relationship and with partner government

Typically long-term timeframe to achieve sustainable capacity development

Establish timelines for remediation and supporting activities over the course of the project

Support partner government leadership in identification and ownership of development agenda

Develop a thorough understanding of technical needs and capacity shortfalls of respective entities

Agree upon the roles and responsibilities of respective stakeholders in implementing and monitoring risk mitigation activities

Provide flexible funding modalities to execute selected projects and activities

Assess and design technical assistance activities to build capacity

Support partner government leadership in identification and ownership of development agenda

Develop a thorough understanding of technical needs and capacity shortfalls of respective entities

Assess and design technical assistance activities to build capacity
How do you incorporate risk responses into the design of development projects?

- Employ ‘work-arounds’ that reduce exposure
- Mitigate and monitor risks
- Develop timeframes for validating improved capacity, reassessing organizational capacity, and audit
- Build capacity in the system
Types of Risk

- Cash Management
- Procurement
- Human Resources
- Institutional Capacity
- IT
- Performance Management
- Value for Money
- Partner and Community Relations
- CSO Vibrancy
- Media Freedom
- Budgeting
- Accounting
- Audit
- PFM Reform Agenda
- Political Environment
- Policy Stance
- Development Interest
- Political Will

Categories:
- Fiduciary
- Programmatic
- Contextual
- Reputational
**Contextual Risk:** Begin considering during development of the CDCS, continue during PAD preparation

**Programmatic Risk:** Identify need for specific analyses in the Concept Paper and conduct analyses (technical capacity, institutional capacity, political will)

**Fiduciary Risk:** Conduct PFMRAF Stage 1, ideally during CDCS development, followed by PFMRAF Stage 2 for each respective government implementing organization; follow-up reviews; pre-award assessments; audit; etc.

**Reputational Risk:** Begin considering during development of CDCS, and examine target partners in PAD prep (DRG Review)

Regardless of when risk is assessed, monitoring and evaluation is continuous
How do we really enable government?

• Ghana decision - through funding at entity (district) level
  “We are doing development, not paying someone else to do it”

• Fiduciary risks
  o Increase – generally less capacity
  o Requires greater involvement from USAID, especially at first
  o Start small to minimize risk exposure

• Reputational risks
  o Directly involved in community development plan
  o Capacity building – Gov’t and USAID, FAR, IL examples

• Programmatic risks
  o More value for money – direct funding
  o Ownership, alignment with government priorities

• Contextual risks
  o Regional unrest
  o Political reality different
  o Personnel movement
Stage 1 Complete ................................................................. 36 Missions
Stage 1 Complete, Stage 2 Initiated ............................... 23 Missions
Reconciling/Waiver .......................................................... 3 Missions

SUMMARY
Lessons Learned

- Partner countries, as well as other donors, welcome our initiative
- Alternatively, a red flag is failure of the partner country to accept our fiduciary responsibility to our taxpayers
- Collaborate and harmonize to reduce partner burden and share the burden and cost of risk management
- It is possible to apply risk management techniques in the public sector.
- It is not easy. Persistence and dedication are key. Respect the power of bureaucracy, but be not defeated by it.
- Mismatch between risk bearing capacity of USG and partner countries
  - Imposes a moral and ethical burden on the risk assessment effort to protect the partner with the lower risk bearing capacity
- Few countries actually ‘fail’ the PFM aspects of PFMRAF, rather the primary inhibitors are democratic accountability limitations
- Believe in the goal of working ourselves out of a job through sustainable development grounded in country ownership.
• Consideration of G2G is based on a holistic project design process that evaluates the most appropriate ways to achieve project purpose and assesses various aspects of risk

• USAID’s risk assessment framework is evolving from a focus on primarily fiduciary risk to a more holistic review that includes reputational, contextual, and programmatic risks

• US GAO and USAID OIG encourage risk management that accounts for broader areas of risk and leverages the work of other partners

• Donors are modernizing risk management through more holistic practices (e.g. World Bank SORT)

• Strengthen collaboration and harmonization with development partners
  – Joint efforts to conduct assessments and capacity building activities
  – Strengthened information sharing and engagement
  – Leveraging technical assistance
Questions?

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