



Office of Inspector General

September 30, 2014

MEMORANDUM

TO: USAID/M/CFO Deputy Chief Financial Officer, Kent Kuyumjian
USAID/Barbados Mission Director, Daniel Smolka
USAID/Dominican Republic Controller, Robert Pedraza
USAID/Honduras Mission Director, James Watson
USAID/Honduras Controller, Robert Arellano

FROM: Regional Inspector General/San Salvador, Van Nguyen /s/

SUBJECT: Review of Stage 2 Risk Assessments for the Latin America and Caribbean Region Under Local Solutions (Report No. 1-598-14-001-S)

This memorandum transmits our final report on the subject review. We carefully considered your comments on the draft report and have included them, without attachments, in Appendix II.

This report contains four recommendations: two to USAID/Barbados, one to USAID/Honduras, and one to USAID/Washington's Bureau for Management, Office of the Chief Financial Officer, Government-to-Government Risk Management Team.

We acknowledge management decisions on Recommendations 1 through 4 and final action on Recommendation 4, which is closed on issuance of this report. Please provide the necessary documentation to obtain final action on the remaining recommendations to the Audit Performance and Compliance Division.

I appreciate the cooperation and courtesy extended to my staff during the review.

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SUMMARY

In August 2010, the USAID Administrator announced a set of reforms known as USAID Forward. USAID Forward promotes

sustainable development through high-impact partnerships and local solutions. In order to achieve long-term sustainable development, we have to support the institutions, private sector partners and civil society organizations that serve as engines of growth and progress for their own nations. USAID Forward is helping us to do that through new models for public-private partnerships and increased investment directly to partner governments and local organizations.¹

The Local Solutions initiative (previously known as Implementation and Procurement Reform) attempts to make foreign assistance more sustainable and cost-effective by building local capacity in the public sector and civil society of partner countries. USAID has already begun simplifying and streamlining policies and procedures to allow it to work with a broader range of non-U.S.-based partners.

In March 2012, USAID issued Automated Directives System (ADS) Chapter 220, “Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance,” to highlight its commitment to partner-country ownership. ADS 220 explains how to determine whether partner-country public financial management (PFM) systems are suitable to implement assistance.

According to ADS 220, USAID missions and operating units should use the Public Financial Management Risk Assessment Framework (PFMRAF) to identify and mitigate the fiduciary risks² encountered when providing government-to-government assistance under Local Solutions. The PFMRAF process, developed by USAID’s Office of the Chief Financial Officer (CFO), includes five stages; the two stages relevant to this review are described below.

Stage 1 Rapid Appraisal. According to ADS 220, the rapid appraisal provides a measure of a prospective partner country’s “commitment to transparency and accountability in the use of public funds.” This appraisal helps the mission decide whether to do the more in-depth Stage 2 PFMRAF risk assessment. In particular, according to the *Public Financial Management Risk Assessment Framework General Guidance* issued by the CFO on September 26, 2012: “The rapid appraisal may inform the areas and/or sectors where Stage 2 Risk Assessment(s) should focus.”

Stage 2 Risk Assessment. According to the General Guidance, during Stage 2 risk assessments, USAID (typically with help from consultants) not only assesses risks but also formulates measures to mitigate them. To do that, USAID should:

¹ “USAID Forward At a Glance,” <http://www.usaid.gov/usaidforward> (accessed on September 23, 2014).

² Fiduciary risk is the danger that funds allocated from the budget may (1) lack proper control, (2) be used for purposes other than those intended, or (3) produce inefficient or uneconomic program results.

- Conduct risk assessments only after spelling out country development objectives, intermediate results, and award mechanisms (contracts, agreements, and grants).
- Examine PFM systems, particularly those for procurement and inventory management. The examination should include limited testing of transactions and review of documents.
- Evaluate and mitigate any risk identified. Mitigation measures can include capacity building and “requirements that government institutions meet specific operational standards prior to receiving fund advances or are subject to close program monitoring for viability and realistic planning.”
- Examine the “current capacity, control systems, and day-to-day practices” associated with the PFM systems used by the ministries, departments, or agencies involved in implementing USAID assistance.
- Complete a questionnaire detailing areas tested and results.

In June 2013, the Office of Inspector General (OIG) issued a *Review of USAID’s Partner-Country and Local Organization Assessments Under Implementation and Procurement Reform*.³ That review covered only one Stage 2 Risk Assessment in the Latin America and Caribbean Region, USAID/Peru. Therefore, RIG/San Salvador performed this review to determine whether other missions in the region conducted their Stage 2 risk assessments to meet the requirements of ADS 220. We chose the three with the most recent Stage 2 risk assessments: Honduras, Barbados, and Trinidad and Tobago.⁴

The review found that missions did not comply with all the risk assessment requirements in ADS 220 (page 4). Examples of shortfalls included the following:

- Risk assessment testing was insufficient (page 4).
- Risk areas identified during the Stage 1 rapid appraisal were not evaluated during the Stage 2 assessment (page 4).
- Stage 2 questionnaires were incomplete (page 5).
- Concerns noted during the Stage 2 risk assessment were not evaluated to mitigate risks (page 5).
- Stage 2 risk assessments were completed before development objectives or projects were identified (page 6).

To mitigate these concerns, we recommend that:

³ *Review of USAID’s Partner-Country and Local Organization Assessments Under Implementation and Procurement Reform*, Report No. 9-000-13-003-S, June 7, 2013.

⁴ The mission in the Dominican Republic is responsible for assessments of Barbados and Trinidad and Tobago.

1. USAID/Barbados update its completed Stage 2 risk assessment by conducting a financial review that tests the effectiveness of operational controls of all PFM systems critical to program implementation and identifies both risks and appropriate risk mitigation actions (page 6).
2. USAID/Barbados assess the potential risk of all the issues noted in work papers but not disclosed or evaluated in the assessment report, and determine what mitigation measures are necessary (page 6).
3. USAID/Honduras implement a risk mitigation plan to address the lack of documentation for the Millennium Challenge Account financial system (page 7).
4. CFO update and reissue Stage 2 guidance to clarify the requirement for a completed questionnaire on any future risk assessments, and other requirements (page 7).

The previous OIG review recommended that the CFO provide more active oversight and add quality assurance controls to the assessment process. Implementation of this recommendation is in process; therefore, we are not making any further recommendations in this area.

Detailed results follow. Appendix I describes the review scope and methodology. Our evaluation of management comments is on page 8, and management's comments appear in their entirety in Appendix II.

REVIEW RESULTS

Risk Assessments Did Not Comply With All Requirements

ADS Chapter 220, “Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance,” provides policy directives and required procedures for determining whether partner-country systems are suitable for implementing USAID-funded assistance. ADS 220 states that approval to use a partner-country system “should be considered on the basis of identified, assessed, allocated and evaluated risk, and if [granted], may contain/be subject to risk mitigation measures to address any such risks.”

The review determined that the Stage 2 risk assessments in Barbados, Honduras, and Trinidad and Tobago did not meet all ADS 220 requirements, as described below.

Risk Assessment Testing Was Insufficient. ADS 220 states that during a Stage 2 assessment, teams

must examine the current capacity, control systems, and day-to-day practices used in the PFM systems in the ministries, departments, or agencies that may be responsible for making and carrying out decisions and actions related to the assistance USAID will provide. . . . this examination should include such tests of PFM systems as necessary to validate the system’s performance and internal controls.

However, the mission assessment teams in Barbados and Trinidad and Tobago did not test to validate the ministries’ systems’ performance and internal controls. The teams reviewed documents—such as reports from accountants and offices of Audit General, and other available research materials—and interviewed personnel at the ministries but did not conduct any testing to confirm that the controls functioned as designed.

Risk Areas Identified During Stage 1 Were Not Evaluated During the Stage 2 Assessment. The General Guidance states: “USAID should evaluate and mitigate any risk identified.” However, in Barbados, the Stage 2 assessment team did not evaluate risks identified in the rapid appraisal.

For instance, the Stage 1 assessment reported that fiscal transparency and internal controls over the procurement system were weak. The Stage 1 assessment also reported the following deficiencies:

- No detailed policies and procedures for procurement.
- No mechanism for complaints, settlement of disputes, or appeals against contract awards.
- No formal process for assessing suppliers’ capabilities for small-value procurements.

However, the assessment team did not evaluate the potential risks associated with these issues during the Stage 2 assessment.

Stage 2 Questionnaires Were Incomplete. The Stage 2 risk assessment guidance requires missions to complete a document called the Stage 2 questionnaire. The questionnaire is a tool that assessment teams use to plan work and document results. However, the guidance does not provide clear instructions on how to complete the questionnaire or the level of detail required. The assessment teams in Barbados and Trinidad and Tobago did not complete all sections of their questionnaires, leaving blank critical sections related to the control environment. Furthermore, simple “no” answers were provided in many sections of the questionnaire, perhaps indicating that controls did not exist. For example, in response to the question “Is there evidence that a risk management process exists and allows management to identify, assess and address existing or potential issues that may hamper the achievement of the entity’s objectives?” one team wrote “no” without further elaboration. The assessment team in Honduras did not answer any sections of the required questionnaire.

Concerns Noted During the Stage 2 Assessment Were Not Evaluated to Mitigate Risks. ADS 220 states:

All risk management decisions should be made on the basis of identified, assessed, and evaluated risk after consideration of the knowledge available at the time of the decision. Risk management decisions may require the partner country government to undertake appropriate risk mitigating actions. . . . Any identified risk must be treated through capacity building, imposition of additional controls, or other measures.

For Barbados, the assessment team identified 16 issues in its questionnaire but did not evaluate their potential risks in order to undertake appropriate risk-mitigating measures. Examples of these issues include the following:

- Fixed-assets registers have not been kept up-to-date.
- Bank reconciliations have not been prepared on schedule because of staffing shortages.
- The Government of Barbados has not completed a formal risk management process.
- Formal procedures to prevent or detect fraud have not been fully implemented.
- There is no system to collect or disseminate procurement data for analysis.

In addition, the risk assessment team in Barbados did not evaluate the potential impact of a scope limitation noted during the Stage 2 assessment—the inability to obtain important documents. Items not available during the testing were (1) documents to confirm the amount of cash available to cover obligations, (2) documents related to the reviews conducted of the procurement system by consultants, and (3) access to the working papers for audits conducted by the Government of Barbados’s Supreme Audit Institution. Lack of access to these documents constituted scope limitations, which the team did not resolve or evaluate as deficiencies.

In Honduras, the assessment team noted that the financial system used by the Millennium Challenge Account⁵ did not have written policies or documentation related to its design, maintenance, or modifications. Furthermore, there was no data backup. The team recommended that the Millennium Challenge Account adopt a different financial system, but the recommended system also lacked documentation related to its design—for example, technical

⁵ The Millennium Challenge Account—Honduras reports to the Office of the President of Honduras. Its purpose is to implement projects funded by the U.S. Government acting through the Millennium Challenge Corporation.

documentation and manuals for users, system administrators, and support staff. The assessment team failed to evaluate the potential impact or provide any mitigation measures to address this risk.

Stage 2 Risk Assessments Were Completed Before Development Objectives Were Identified. The Stage 2 assessment guidance requires the risk assessments to be conducted after the mission has set out its country development objectives, intermediate results, and award mechanisms.

However, the Stage 2 risk assessments for Barbados, Honduras, and Trinidad and Tobago were completed before the missions completed their Country Development Cooperation Strategies and laid out the development objectives and other requirements.

The CFO revised the guidance and ADS 220 in July 2014 after our review was conducted to clarify how the PFMRAF and the design process relate to one another. The guidance no longer requires that country development objectives, intermediate results, and award mechanisms be completed prior to conducting a Stage 2 assessment; therefore, we are not making a recommendation on this issue.

These identified weaknesses occurred because missions lacked experience with Stage 2 risk assessments. Furthermore, the written guidance provided to the missions was not clear on what type of testing they should conduct although it required “sufficient testing,” which was not defined. Additionally, although the guidance requires testing and evaluation of previous risk assessments when they are used as part of the Stage 2 risk assessment, it does not explain how to carry them out or how to weigh assessment factors to compare results. The guidance was not clear on the type of testing or other requirements because USAID’s administration was strongly pushing for increased Agency-wide government-to-government assistance, and the assessment framework had to be constructed while it was being deployed. Finally, the quality control reviews that the CFO’s office completed—according to ADS 220, a support team within the CFO’s office “ensures quality control and consistency in using the PFMRAF”—were done quickly and did not identify the problems with the assessments done by Barbados or Honduras nor provided needed guidance to strengthen the assessment process. The previous OIG review recommended that the CFO provide more active oversight and add quality assurance controls to the assessment process. Implementation of this recommendation is in process; therefore, we are not making any further recommendations in this area.

Approving the use of PFM systems without adequately validating their overall operations, risks, and internal controls puts USAID funds at risk. To mitigate the concerns noted during the review, we make the following recommendations.

Recommendation 1. *We recommend that USAID/Barbados update its completed Stage 2 risk assessment by conducting a financial review that tests the effectiveness of operational controls of all public financial management systems critical to program implementation and identifies both risks and appropriate risk mitigation actions.*

Recommendation 2. *We recommend that USAID/Barbados assess the potential risk of all the issues noted in work papers but not disclosed or evaluated in the assessment report, and determine what mitigation measures are necessary.*

Recommendation 3. *We recommend that USAID/Honduras implement a risk mitigation plan to address the lack of documentation for the Millennium Challenge Account financial system.*

Recommendation 4. *We recommend that the Office of the Chief Financial Officer update and reissue Stage 2 guidance to clarify the requirement for a completed questionnaire on any future risk assessments, and other requirements.*

EVALUATION OF MANAGEMENT COMMENTS

In its comments on the draft report, USAID/Barbados, USAID/Honduras, and the CFO agreed with all but one of what were then five recommendations. We reviewed management's comments and the supporting documentation provided and agreed to delete Recommendation 5 from the final report. We acknowledge management decisions on Recommendations 1 through 4 and final action on Recommendation 4. A detailed evaluation of management comments follows.

Recommendation 1. USAID/Barbados decided to perform a financial review of the public financial management system of the Ministry of the Environment and Drainage. The mission anticipated completing this review by December 31, 2014. We acknowledge management's decision.

Recommendation 2. USAID/Barbados decided to perform a review of all the issues noted in the working papers that were not disclosed or evaluated in the assessment report, focusing on those with major impact on operations and other critical functions. The mission anticipated completing this review by December 31, 2014. We acknowledge management's decision.

Recommendation 3. USAID/Honduras decided that, instead of implementing a plan to address the lack of documentation, it would include the required documentation of the financial system in the next work plan. It further decided to include the documentation in the user manual by December 31, 2014. We acknowledge management's decision.

Recommendation 4. The CFO has revised ADS 220 and the Agency policy directive governing the PFMRAF, effective July 28, 2014. The policy requires the Stage 2 questionnaire as a step in completing the Stage 2 risk assessment. In addition, the PFMRAF manual is a mandatory reference to the policy and requires completion of the questionnaire as a primary source of evidence for the assessment. We acknowledge the mission's management decision and final action.

SCOPE AND METHODOLOGY

Scope

The review was conducted in accordance with the Council of the Inspectors General on Integrity and Efficiency's 2012 *Quality Standards for Inspection and Evaluation*.

We performed this review as a follow-up to a report issued by OIG's Performance Audits staff titled *Review of USAID's Partner-Country and Local Organization Assessments Under Implementation and Procurement Reform*, June 2013. The Regional Inspector General/San Salvador conducted this review to determine whether missions in the Latin America and Caribbean Region conducted Stage 2 risk assessments to address the requirements of ADS 220.

In planning and performing the review, we obtained a listing of all Stage 2 risk assessments completed in the region and selected a sample of the three most recent ones from: Honduras, Barbados, and Trinidad and Tobago. The review team obtained documentation supporting the missions' approval of the use of partner-country public financial management systems. The team reviewed the Stage 1 rapid appraisal, the questionnaire supporting the work done by the missions, concept papers, award documentation, statements of work, risk mitigation plans, Country Development Cooperation Strategies for the countries evaluated, and other reports.

We reviewed regulations as well as USAID guidelines pertaining to the use of reliable partner-country systems and Stage 2 risk assessments, including ADS 200 and supplemental guidance. The review relied on the following sources of evidence: Stage 2 risk assessment reports, interviews with the controllers' offices in Honduras and Dominican Republic (the controller's office in the Dominican Republic is responsible for overseeing any Stage 1 or Stage 2 assessment for Barbados and Trinidad and Tobago), and documentation maintained by the CFO in Honduras and Dominican Republic. We conducted fieldwork from January 20 through February 7, 2014.

Methodology

To answer the review objective, we conducted interviews and reviews of supporting documentation. We evaluated the oversight by the CFO of the risk assessments. We also reviewed documentation supporting prospective projects considered by the missions.

Through these interviews and the review of project documentation, the review team determined whether (1) the assessment included testing of PFM systems as necessary to validate overall operations and internal controls, (2) the Partner Country Systems team had gathered evidence that the PFM systems were of acceptable quality, (3) the Partner Country Systems team had evaluated the day-to-day practices in the applicable ministries, (4) missions had identified their development objectives prior to the Stage 1 rapid appraisal, and (5) missions had identified and evaluated vulnerabilities in the PFM system.

MANAGEMENT COMMENTS



USAID
FROM THE AMERICAN PEOPLE

Barbados and the Eastern Caribbean

MEMORANDUM

Date: August 11, 2014
To: Regional Inspector General/San Salvador, Van Nguyen
From: Mission Director, USAID/BEC, Jonathan Conly /s/
Through: USAID Regional Controller, Robert Pedraza /s/
CC: USAID/M/CFO, Deputy Chief Financial Officer, Kent Kuyumjian
Subject: Mission Comments on Review of Latin America and Caribbean Region, Stage 2 Risk Assessments Under Implementation and Procurement Reform

On July 22, 2014, RIG/San Salvador issued its draft report of the Review of Latin America and Caribbean Region Stage 2 Risk Assessments and requested the Mission to provide its review and comments. The draft report included two recommendations, listed below, which the Mission desires to respond to in the following manner:

Recommendation 1. USAID/Barbados update its completed Stage 2 risk assessments by doing a financial review that tests the effectiveness of operational controls of all PFM systems critical to program implementation and identifies both risks and appropriate risk mitigation actions (page 6).

Mission comments- USAID/Barbados agrees with the recommendation and wishes to offer the following clarifications and comments on implementing the recommendation. The Mission notes that in performing the Stage 2 Risk Assessment for Barbados, it sought and followed the CFO guidance that was available at that time. Subsequent to completion of the Stage 2 Risk Assessment for Barbados, the Mission entered into an agreement with the Government of Barbados (GOB) for a climate change adaptation activity to be implemented through the Ministry of Environment and Drainage. USAID/Barbados will perform a Financial Review of the Public Financial Management System as relevant to the Ministry of the Environment and Drainage in implementing the USAID activity. We anticipate completing this assessment by December 31, 2014.

Recommendation 2. USAID/Barbados assess the potential risk of all the issues noted in work papers but not disclosed or evaluated in the assessment report, and determine what mitigation measures are necessary (page 6).

Mission comments – USAID/Barbados agrees with the recommendation and wishes to offer the following clarifications and comments on implementing the recommendation. The Mission will perform a Review of all issues noted in working papers, but not disclosed or evaluated in the

assessment report, with Mission's emphasis on identifying issues with major impact on operations or other critical functions, and focusing on matching these with appropriate actions and/or mitigation measures. We anticipate completing this action(s) by December 31, 2014.

The draft report also included a recommendation for the Office of the Chief Financial Officer. Because this recommendation relates to USAID/Barbados and specifically to the factual background to USAID/Barbados' Stage 2 Risk Assessment, we wish to offer a clarification in this regard.

Recommendation 5. USAID/M/Office of Chief Financial Officer issue written notice to missions not to proceed with Stage 2 risk assessments until development objectives, intermediate results, and award mechanisms are completed (page 7).

Mission Comments – Although this recommendation is to the CFO rather than to USAID/Barbados, we believe, it is important to note that USAID/Barbados did have a specific development objective formulated prior to undertaking the PFMRAF process with the GOB.

The draft report indicates that the Stage 2 risk assessment for Barbados was completed before the Mission completed its Country Development Cooperation Strategy (CDCS) and laid out the development objectives and other requirements. At the time USAID/Barbados and Eastern Caribbean started the PFMRAF process, it did have in place a five year (2011-2015) strategy, approved by the LAC Bureau, and a defined Development Objective of **Risks to Human and Natural Assets Resulting from Climate Variability Reduced**. It also had in place an Activity Approval Document (AAD) for the climate change development objective and had identified the Government of Barbados as a potential implementing partner. Thus, although the Mission did not yet have a CDCS, *per se*, approved (it is now working on finalizing a Regional Development Cooperation Strategy since the Mission manages a regional program), it was operating under an approved strategy with defined objectives and intermediate results. For that reason, we believe the risk assessment process was appropriately targeted to a planned activity.

USAID/Barbados appreciates the RIG's consideration of the Mission's comments on these recommendations and look forward to receiving the final audit report. Please let us know if you need any additional information.

**MEMORANDUM**

28 August 2014

TO: Regional Inspector General/San Salvador, Van Nguyen**FROM:** James Watson, Mission Director /s/**SUBJECT:** Management Response to Draft Audit of Latin America and Caribbean Region Stage 2 Risk Assessments" (Report No. X-XXX-XX-XXX-X).

Thank you for the opportunity to respond to the draft audit report on the *Audit of Latin America and Caribbean Region Stage 2 Risk Assessments* and for the professionalism exhibited by your staff throughout the audit. Below, please find our comments and management decisions regarding the proposed audit recommendation:

Recommendation 3: USAID/Honduras implement a risk mitigation plan to address the lack of documentation for the financial system.

Management Comments: The mission agrees with the recommendation, and the following steps constitute the implementation of the risk mitigation plan. Millennium Challenge Account-Honduras (MCA-H) – also known as INVESTH- is in the process of documenting and creating user manuals for SIGMA, their accounting system. This system interfaces with the Government of Honduras's national system, SIAFI. Once completed, this documentation will eliminate the weakness identified by the Stage 2 Assessment.

The requirement to document SIGMA is being included in the next work plan, which is expected to be finalized in early September, 2014. In addition, the work plan will ensure adequate safeguards for the time period prior to full documentation of SIGMA. These steps will include ensuring that SIGMA has adequate backups of financial and other project information, proper physical security of IT equipment, and other steps as deemed appropriate. The AOR will ensure full compliance with this section of the approved work plan via regular site visits. In the previous progress report, verified by the AOR, MCA-H reported that they have already developed modules in SIGMA to produce financial information required under their agreement with USAID. The documentation for this process will be included in the user manual, which is expected to be finalized before the end of 2014.

Target Completion Date: December 31, 2014



MEMORANDUM

TO: Regional Inspector General/San Salvador, Van Nguyen

FROM: Reginald W. Mitchell, Chief Financial Officer (M/CFO) /s/

SUBJECT: Management Response to Draft Audit of "Latin America and Caribbean Region Stage 2 Risk Assessments" (Report No. X-XXX-XX-XXX-X).

Thank you for the opportunity to respond to the draft audit report on the *Audit of Latin America and Caribbean Region Stage 2 Risk Assessments* and for the professionalism exhibited by your staff throughout the audit. In the future, please ensure that all audit reports specific to the Office of the Chief Financial Officer (CFO) are addressed directly to Reginald W. Mitchell, Chief Financial Officer, M/CFO. Our comments and management decisions regarding the proposed audit recommendations follow:

Recommendation 4: We recommend that the Office of the Chief Financial Officer update and reissue guidance to clarify the requirement for a completed questionnaire on any future risk assessments.

Management Comments: We agree with the recommendation. ADS 220, *Use and Strengthening of Reliable Partner Government Systems for Implementation of Direct Assistance*, and the agency policy directive governing the Public Financial Management Risk Assessment Framework (PFMRAF) was revised effective July 28, 2014. The policy requires the Stage 2 questionnaire as a step in completing the Stage 2 Risk Assessment; and the PFMRAF Manual which provides implementation guidance and is a mandatory reference to the policy, elaborates completion of the questionnaire as primary source of evidence for the assessment.

Specifically, the policy includes language requiring the Mission or Operating Unit to develop a list of PFM risk assessment evaluation criteria (Stage 2 questionnaire) to guide the risk assessment. The questionnaire presents a comprehensive list of questions by function, criterion and sub-criteria as a starting point to be evaluated as part of the Stage 2 assessment. The questionnaire need not be used in its entirety, but rather focused on the areas and questions considered relevant and within the scope of the respective Stage 2 risk assessment. Assessment teams may draw from other professional guidelines or checklists to develop a customized questionnaire. The PFMRAF Manual elaborates that if the questionnaire is customized, the assessment team should document the rationale and specifics of changes made. Further, completion of the questionnaire will become the primary source of evidence for the Stage 2 Risk Assessment. Moreover, the existing format of the questionnaire should be logically cross-walked or referenced to support information included in the Stage 2 Risk Assessment report.

Based on the substantive revisions to the policy and implementation guidance, we request the OIG consider this recommendation closed upon issuance of the audit report.

Target Completion Date: M/CFO requests closure upon issuance of the final report.

Recommendation 5: We recommend that the Office of the Chief Financial Officer issue written notice to missions not to proceed with Stage 2 risk assessments until development objectives, intermediate results, and award mechanisms are completed.

Management Comments: We do not agree with this recommendation and recommend its removal. The July 28, 2014 revision of ADS 220, *Use and Strengthening of Reliable Partner Government Systems for Implementation of Direct Assistance* addresses and enhances the relationship between the Public Financial Management Risk Assessment Framework (PFMRAF) and the latest version of ADS 201, *Planning*, which contains the Agency's project design guidance. The revision also clarifies that the PFMRAF Stage 2 – Risk Assessment process includes the following step: At the Concept Paper Stage of project design, the Mission, Project Design Team, and Partner Government Systems team members identify a clear statement of the project purpose (aligned with an Intermediate Result in the Country Development Cooperation Strategy (CDCS) results framework) and identify the partner government entity counterparts. In addition, ADS 220 (version 3) stipulates that the Stage 2 – Risk Assessment should not be implemented unless it is part of a broader project design process, documented by an approved Concept Paper. Therefore, the country development objectives, intermediate results and award mechanisms need not be finalized when the Stage 2 –Risk Assessment is being conducted ADS 220 describes PFMRAF as a management assessment tool that informs and is part of project design. ADS 201 details project design requirements, including the link between the Results Framework and Logical Framework. ADS 201 also includes the CDCS process, which requires identification and completion of development objectives and intermediate results. Though the PFMRAF may inform the CDCS as appropriate, it is neither required nor designed to inform or influence development objectives or intermediate results. Missions considering the use of partner government institutions for implementation should strive to complete Stage 1 Rapid Appraisal (or revisions thereto) in conjunction with the development or revision of the CDCS. Stage 2 Risk Assessments may commence any time a partner government entity has been identified in an approved Concept Paper as being actively considered as an implementing entity. Timing is otherwise at the Mission's discretion. CDCS is overseen by the Office of Program, Policy, and Learning (PPL). The Office of the Chief Financial Officer (CFO), specifically the Government-to-Government Risk Management Team (G2GRMT), provides quality control and oversight of the PFMRAF process. It would be inappropriate for CFO or G2GRMT to make determinations related to development objectives, intermediate results and/or policy thereof which are outside of their purview.

The reference to award mechanisms is confusing and appears out of context. G2G funding mechanisms with partner governments are not awards, which relate to contractual arrangements. Though specific G2G mechanisms may be envisioned at the time of Stage 2 Risk Assessment(s), the choice of mechanism need not be determined at this stage and indeed are often finalized with project design. Thus, it would be inappropriate for Missions to finalize a funding mechanism before the Stage 2 Assessment is initiated.

Based on the above discussion, we request that RIG close this finding upon issuance of the audit report, as the recommendation has been addressed.