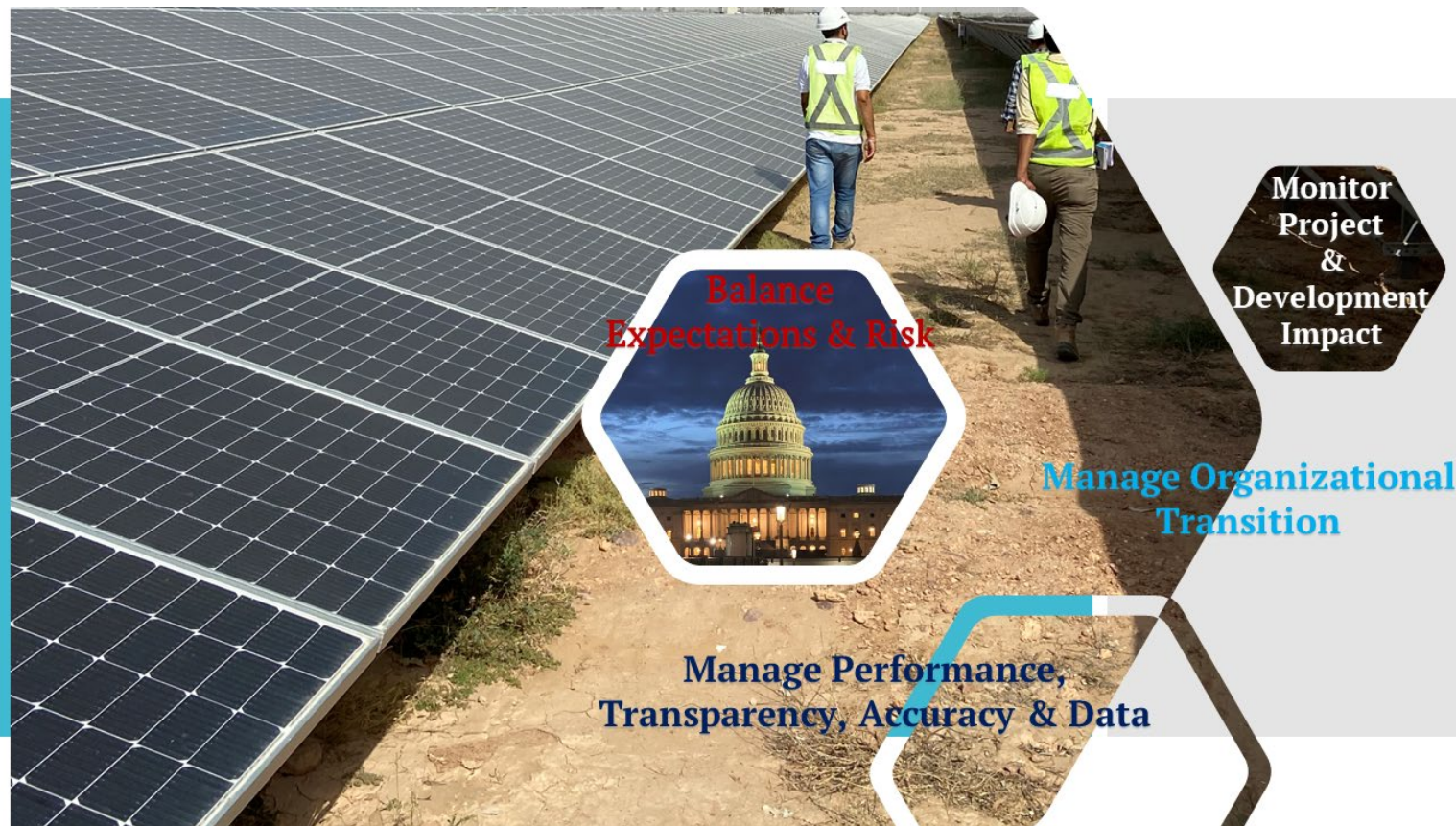




**U.S. International Development Finance Corporation
Office of Inspector General**

Top Management Challenges Facing DFC in FY 2023



**Balance
Expectations & Risk**

**Monitor
Project
&
Development
Impact**

**Manage Organizational
Transition**

**Manage Performance,
Transparency, Accuracy & Data**

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TABLE OF CONTENTS

| | |
|---|-----------|
| MESSAGE FROM THE INSPECTOR GENERAL | 4 |
| INTRODUCTION..... | 8 |
| 1. Improving Monitoring and Evaluating Actual Development Impact..... | 10 |
| 2. Improving Performance Management, Transparency, Accuracy, and Availability of Project Data as DFC’s Commitments Grow..... | 12 |
| 3. Balancing Heightened Expectations of Congress and Stakeholders While Managing Risks..... | 14 |
| 4. Managing Organizational Transition While Building Internal Controls Around Core Management Systems..... | 16 |
| CONCLUSION | 18 |
| MANAGEMENT’S COMMENTS..... | 19 |



MESSAGE FROM THE INSPECTOR GENERAL



Anthony "Tony" Zakel, Inspector General

The U.S. International Development Finance Corporation (DFC) was created by the Better Utilization of Investments Leading to Development Act of 2018 ([BUILD Act](#)), and is authorized until October 2025. DFC began operations in January 2020,¹ consolidating the functions of its predecessor agencies, the Overseas Private Investment Corporation (OPIC) and the U.S. Agency for International Development's (USAID) Development Credit Authority (DCA). DFC partners with the private sector to finance solutions to the most critical challenges facing the developing world today, thereby advancing economic growth and promoting U.S. national security interests.

DFC supports development projects in a variety of sectors, including energy, healthcare, and infrastructure, by providing equity and debt financing, political risk insurance, and technical assistance. Through the BUILD Act, DFC was granted an expanded lending capacity of \$60 billion and a more focused mission on development impact in lower income and lower-middle income countries. DFC had a portfolio of more than \$35 billion in FY 2022 and added total new commitments of more than \$7 billion in FY 2022, which was a record year for DFC (OPIC previously averaged around \$4.5 billion of new commitments each year). DFC aims to mobilize additional private sector capital – for a total of \$75 billion – to reach more than 30 million people by the end of 2025. In FY 2022, projects supported by DFC helped combat the effects of climate change, the COVID-19 pandemic, gender inequality, and food insecurity.

DFC Office of Inspector General (OIG) provides independent oversight of DFC programs and operations through audits and investigations designed to prevent waste, fraud, and abuse in DFC

¹ Because DFC did not have appropriated budgetary authority until January 1, 2020, the FY 2020 first quarter projects were assigned to OPIC because those projects were authorized and OPIC appropriations was used to commit those projects

programs, and promote economy, effectiveness, and efficiency in DFC operations.² This helps ensure the U.S. Government supports economic growth, promotes U.S. national security interests, and maximizes return on investments. As part of this oversight, the Reports Consolidation Act of 2000 requires federal agencies to include in their performance and accountability reports a statement by their Inspector General summarizing the most serious management and performance challenges facing the agency, and progress in addressing those challenges.³

The results of recent DFC OIG audits and investigations, as well as our March 2022 correspondence to the newly appointed DFC CEO⁴ have revealed the following four Top Management Challenges (TMCs) facing DFC in FY 2023. These challenges are similar to TMCs identified in FY 2022.⁵ This is not surprising given that DFC is a new and evolving organization. Indeed, we expect these challenges to continue over the next several years. The TMCs we have identified for FY 2023 are:

- 1. *Improving Monitoring and Evaluating Actual Development Impact.*** DFC has made some progress in this area, particularly in estimating development impact as part of its investment decision-making process. However, DFC must find appropriate methods to oversee projects to ensure it meets development impact goals as it progresses through completion. DFC still relies primarily on client self-reporting. Now that COVID-19 pandemic related travel restrictions have been lifted, and as DFC continues to increase the size of its investment portfolio, DFC must take action to make actual development impact achieved and promotion of our nation’s foreign policy the primary metrics of its success.
- 2. *Improving Performance Management, Transparency, Accuracy, and Availability of Project Data as DFC’s Commitments Grow.*** The BUILD Act requires DFC to create a performance measurement system to evaluate and monitor projects, and to guide plans for future projects. The BUILD Act also requires DFC to prioritize investment in lower income countries (LICs) and lower middle-income countries (LMICs). DFC has also deployed a new system to track the receipt, review, and certification of all project deliverables and is currently working to improve monitoring projects and reporting borrower evaluations. However, our BUILD Act audit found that DFC had not finalized and communicated its FY 2022 financial performance standards for its portfolio.
- 3. *Balancing Heightened Expectations of Congress and Stakeholders While Managing Risks.*** DFC has many stakeholders, both in the United States and around the world, who are interested in what it does and how it achieves its goals. DFC also faces difficult choices in making investments that balance the competing interests of development impact, foreign policy, and financial performance. Finding the proper balance between these competing priorities presents a significant challenge. DFC OIG believes DFC will continue to face significant challenges in the constantly evolving global environment to advance

² The BUILD Act created a dedicated DFC Office of Inspector General (DFC OIG), which derives its authority from the Inspector General Act of 1978, as amended ([IG Act](#)).

³ Reports Consolidation Act of 2000, ([Public Law 106-531](#)), section (5)(b), states: “[E]ach program performance report shall contain an assessment by the agency head of the completeness and reliability of the performance data included in the report. The assessment shall describe any material inadequacies in the completeness and reliability of the performance data, and the actions the agency can take and is taking to resolve such inadequacies.” Although DFC does not fall under the jurisdiction of the Reports Consolidation Act, DFC OIG proactively publishes its Top Management Challenges each fiscal year as a government-wide best practice.

⁴ [DFC OIG Letter to DFC CEO Scott Nathan](#), March 21, 2022.

⁵ [Top Management Challenges Facing DFC in FY 2022](#).



development through its investments while meeting the heightened expectations of Congress and other stakeholders.

4. *Managing Organizational Transition While Building Internal Controls Around Core Management Systems.* DFC inherited many talented and experienced employees from its predecessor agencies, OPIC and DCA and plans to dramatically grow its workforce to 700 staff by September 2023. However, DFC faces recruitment challenges. Although DFC is the United States' development financial institution, it does not offer the higher pay rates of other federal financial institutions, such as the Federal Deposit Insurance Corporation, the Federal Reserve, the Federal Housing Finance Agency, and the National Credit Union Administration. The OIG has also identified internal control weaknesses through our audit of DFC's purchase card program and Federal Information Security Modernization Act of 2014 (FISMA) compliance. Managing a transition to a larger organization while strengthening its internal controls and management systems will continue to be a challenge as DFC grows.

Each challenge is discussed in greater detail in this report. Please contact me if you would like to discuss or have any questions.

Sincerely,

A handwritten signature in blue ink, reading "Anthony Zakel".

Anthony "Tony" Zakel
Inspector General

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INTRODUCTION

The BUILD Act provided DFC with new and innovative financial products to bring private capital to the developing world. These development finance tools, such as loans, guarantees, equity, and political-risk insurance, will facilitate private sector investment in developing countries that will have a positive – and measurable – developmental impact. DFC facilitates transactions the private sector would not otherwise conduct due to heightened risks in developing countries. Limited backing from the U.S. Government (USG) can help catalyze significant amounts of private capital into these countries. This backing is essential to supporting key sectors, such as power, energy, water, infrastructure, agriculture, and health, which improve the quality of life for millions and lay the groundwork for creating modern economies and providing financing for women or other borrowers who do not have sufficient access to commercial financing.

In accordance with the BUILD Act, DFC provides developing countries a robust alternative to state-directed investments by authoritarian governments and U.S. strategic competitors. DFC incentivizes private sector-led development projects in developing countries that adhere to high standards and are financially viable over the long term, while ensuring that contracts are transparent and that transactions properly address economic and social impacts. This encourages more American businesses to invest in developing markets, including those of key national security importance to the United States.

DFC has identified four key goals in its latest Strategic Plan⁶ to drive the next chapter of its growth.

GOAL 1: Engage and Mobilize the Private Sector.

“DFC’s targeted outcome for this strategic goal is to mobilize private capital in support of sustainable, broad-based economic growth, and poverty reduction that advances development and U.S. foreign policy interests.”

GOAL 2: Drive Development Impact Across Sectors and Regions.

“There are several targeted outcomes of this strategic goal:

1. Increase development outcomes in each of the following development sectors [: energy, health, digital, housing, infrastructure, food security and agriculture, and water, sanitation, and hygiene].

⁶ [DFC Strategic Plan FY 2022-2026](#)



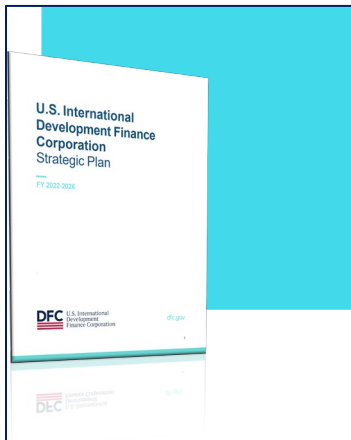
2. Craft a well-balanced portfolio across regions that aligns with USG development and national security priorities.
3. Increase exposure to investments that help combat the effects of climate change, increase financial inclusion in developing markets, and increase equity and inclusion.”

GOAL 3: Impact Management Monitoring, Measurement, and Learning.

“DFC is building up its new Impact Management, Monitoring, and Learning (IMML) division to strengthen its ability to monitor, analyze, and manage the development impact of its portfolio on an ongoing basis, compare objectives and targets to actual results, suggest adjustments where needed, and identify learnings [sic] that help improve new and existing projects.”

GOAL 4: Scale the Corporation Sustainably.

“The increase in tools, capacity, and complexity [brought about by the merger of OPIC and USAID’s financing arm, and the BUILD Act’s increased investment capacity] requires supporting people and processes to grow its ability to fulfill BUILD Act mandates, prudently manage its portfolio, and efficiently execute on new project activity.”



DFC’s first goal is aimed at fulfilling DFC’s core mission. DFC’s second goal derives from a combination of its BUILD Act mandate and the current Administration’s policy. DFC’s third goal aligns directly with one of our TMCs – improving monitoring and evaluating actual development impact. DFC’s fourth goal aligns broadly with another of our TMCs – managing organizational transition while building internal controls around core management systems. Thus, DFC’s strategic goals align with its mission and some of the challenges discussed in this report.

Source: DFC Website www.dfc.gov



1. Improving Monitoring and Evaluating Actual Development Impact.

The BUILD Act requires that DFC develop standards and methods for ensuring development performance, including measurement of the projected and actual development impact of a project. In September 2022, DFC OIG published an audit, [DFC Made Significant Progress Implementing Provisions of the BUILD Act](#), and found that DFC had not yet reported actual development impact on a country-by-country basis. A related issue was also identified in a previous USAID OIG audit in February 2019, which found that data captured by OPIC was insufficient to measure the development impact created by the effects of the projects it supported.

DFC has made some progress in this area, particularly in estimating development impact as part of its investment decision-making process. As required under the BUILD Act, DFC developed a performance management tool, the Impact Quotient (IQ), which DFC uses to estimate, monitor, and evaluate project development impact. However, DFC must find appropriate methods to oversee projects to ensure it meets development impact goals as it progresses through completion. DFC still relies primarily on client self-reporting. In some instances, this has allowed extensive fraud to go undetected. One example is the Kabul Marriott Hotel, where an investigation by the Special Inspector General for Afghanistan Reconstruction (SIGAR) revealed an \$85 million fraud perpetrated against OPIC due to lack of site visits and on-site monitoring.

In addition, there have been recent concerns, including in Congress, regarding the negative impact of microfinance on the well-being of borrowers who have faced aggressive debt-collection tactics by governments and private lenders. Given the significant size of DFC's microfinance loans portfolio, we have included a review of these types of loans in the current audit of DFC policies, procedures, and processes.⁷ Our audit will also address, among other items, microfinance and renewable energy (solar) projects in India. Project monitoring and evaluation are critical to ensure that partner finance institutions implement safeguards to protect DFC-supported projects from conduct that is illegal, unethical, or contrary to USG policy.

⁷[DFC OIG Audit Announcement Letter- India Renewable Energy and Financing Projects](#), June 7, 2022



Engagement with DFC beneficiaries is also critical to ensure the intended purpose of the investment. Now that COVID-19 pandemic related travel restrictions have been lifted, and as DFC continues to increase the size of its investment portfolio, DFC must take action to make actual development impact achieved and promotion of our nation’s foreign policy the primary metrics of its success. In my tenure as Inspector General, on-site project monitoring and measuring actual impact are the areas where DFC can make the most improvement.

Map of DFC New Transactions in Low and Lower-Middle Income Countries



Source: DFC 2021 Annual Report

2. Improving Performance Management, Transparency, Accuracy, and Availability of Project Data as DFC's Commitments Grow.

While DFC has made progress in its performance management, it remains a challenge for DFC to meet the requirements of both the Foundations for Evidence-Based Policymaking Act of 2018 ([Evidence Act](#)) and the Government Performance and Results Act Modernization Act of 2010 ([GPRAMA](#)). The Evidence Act, as [interpreted by the Office of Management and Budget \(OMB\)](#), requires that federal agencies collect and assure they have quality data to make informed policy decisions and determine whether they are achieving their essential mission. The GPRAMA requires federal agencies to show mission achievement and create a culture where data and empirical evidence play a greater role in policy, budget, and management decisions. Specifically, GPRAMA requires agencies to develop a performance management framework that includes strategic plans, performance plans, and performance reports.

Previous audits have identified areas to improve DFC's broader performance management framework, as well as measure the projected effects of development projects. The BUILD Act requires DFC to create a performance measurement system to evaluate and monitor projects, and to guide plans for future projects. The BUILD Act also requires DFC to prioritize investment in lower income countries (LICs) and lower middle-income countries (LMICs), while also supporting U.S. economic and foreign policy interests. DFC established internal goals for increasing the number of projects in LICs/LMICs in its [Roadmap for Impact](#) and established an internal target of 60 percent of the private sector projects it commits will be in LICs, LMICs, and fragile states.

DFC has also deployed a new system to track the receipt, review, and certification of all project deliverables within its Insight System and is currently working to improve monitoring projects and reporting borrower evaluations. Our BUILD Act audit found that DFC had not finalized and communicated its FY 2022 financial performance standards for its portfolio. We found that, in FY 2021, DFC exceeded the 60 percent target for the number of projects in LICs and LMICs, and, as of May 2022, DFC's new project pipeline in LICs and LMICs is more than 60 percent of its new projects and dollar commitments. However, we found that DFC does not have a consistent methodology for tracking progress towards the internal 60 percent target. A



previous USAID OIG audit noted that OPIC’s performance management framework lacked the rigor needed to assess progress in advancing its mission, with staff noting that tracking the progress of strategic goals was ad hoc at best, if done at all.

The third goal of DFC’s Strategic Plan is to improve impact management, monitoring, measurement, and learning. DFC has made changes within its Office of Development Policy to achieve this goal. Specifically, it formed the Impact Management, Monitoring, and Learning (IMML) division and has given IMML overall responsibility for certain project oversight tasks. Assuming IMML is properly staffed and empowered, this should allow DFC to strengthen its monitoring and oversight of projects.

Crowded and Sometimes Conflicting DFC Stakeholder Environment



3. Balancing Heightened Expectations of Congress and Stakeholders While Managing Risks.

One of the main reasons the BUILD Act enjoyed bipartisan support was the widely held belief that the United States needed to do more to counter the global development influence of the People’s Republic of China (PRC) and, to a lesser extent (at that time), Russia. Achieving such foreign policy goals, however, can sometimes conflict with fulfilling DFC’s core development mission. On the one hand, DFC’s statutory mandate is to prioritize the economic development of less developed LICs and LMICs. On the other hand, advancing foreign policy goals may require investments in more developed countries.

DFC has many stakeholders, both in the United States and around the world, who are interested in what it does and how it achieves its goals. These stakeholders expect DFC to provide developing countries with a robust alternative to state-directed investments by authoritarian governments and U.S. strategic competitors. In addition, DFC has assumed expectations and responsibilities for making equity investments (through the BUILD Act), and for supporting certain energy-related investments in eligible European and Eurasian high-income countries (through the European Energy Security and Diversification Act of 2019).⁸ The recently launched G7 Partnership for Global Infrastructure and Investment aims to mobilize \$600 billion by 2027 in global infrastructure investments. The plan published by the Biden Administration contains specific investment initiatives for DFC, including technical assistance grants, debt financing, and capital investments in climate-sustainable ventures.⁹ There is also discussion to increase DFC’s portfolio through various legislative proposals. Although DFC products have expanded, the current budget treatment of equity investments hinders DFC in making a larger

⁸ DFC investments in upper-middle income countries focus on reaching underserved populations including women and people living in rural areas, [DFC: Investing in Global Development](#).

⁹ [FACT SHEET: President Biden and G7 Leaders Formally Launch Partnership for Global Infrastructure and Investment](#), June 26, 2022



impact with equity investments, particularly in infrastructure. DFC is currently working with Congress and OMB to address this issue.

DFC faces difficult choices in making investments that balance the competing interests of development impact, foreign policy, and financial performance. Finding the proper balance between these competing priorities presents a significant challenge – a challenge compounded by the fact that the PRC is the major creditor in the developing world. According to a World Bank report, of the \$35 billion that the world’s 74 lowest-income nations will owe in debt service payments this year, \$13.1 billion – or about 37 percent – is owed to PRC entities.

In addition to competing priorities, recent world events, particularly the Russian invasion of Ukraine, have led Congress and stakeholders to request additional DFC support in eastern Europe and Eurasia to reduce dependence upon Russian energy exports. Meanwhile, in accordance with the BUILD Act, DFC is required to be values-based and must hold its project sponsors to higher standards for integrity and compliance with environmental, social, and governance standards than its strategic competitors. In addition, DFC cannot move as quickly as many of its strategic competitors because it is required to follow certain BUILD Act and other procedural requirements, including congressional notifications, for projects over certain thresholds.

DFC also faces challenges when investing in LICs and LMICs because development projects in these countries tend to be smaller and higher risk, requiring more resources and human capital to conduct due diligence reviews and investment decision-making. Currently, the economies of some LICs and LMICs have been pushed to the brink due to the COVID-19 pandemic, and now, with the Russian invasion of Ukraine, the effect of higher food prices is being felt acutely as food accounts for a higher share of income in these countries. Inflation, along with rising levels of debt, are creating financial stress on the economies of some of these countries. And unlike more developed countries some LICs and LMICs do not have large domestic markets to aid in economic recovery. The International Monetary Fund’s Chief Economist recently opined that the world may soon be teetering on the edge of a global recession, and that rising food and energy prices could cause widespread food insecurity and social unrest.

DFC is taking steps to mitigate these risks, including deploying personnel overseas to ensure closer collaboration with U.S. Embassy and USAID mission staff and to have greater visibility of local opportunities. In addition, DFC has created the Development Finance Fellows program, which helps USAID and State Department Foreign Service Officers develop an understanding of the DFC investment process, products, and services. DFC is also working with an independent contractor to evaluate opportunities and challenges facing DFC in LICs, thereby taking significant steps to address the challenges inherent in investing in the developing world. DFC OIG believes DFC will continue to face significant challenges in the constantly evolving global environment to advance development through its investments while meeting the heightened expectations of Congress and other stakeholders.



4. Managing Organizational Transition While Building Internal Controls Around Core Management Systems.

DFC inherited many talented and experienced employees from its predecessor agencies, OPIC and DCA. However, the creation of a new agency with a new mandate from the consolidation of two agencies, each with its own mission and culture, presents a significant management challenge. Strong leadership is needed to continue blending the two predecessor agencies into a new organization with an expanded mission and its own culture. As DFC grows both in staff and portfolio size, DFC must be vigilant to ensure it has strong and effective internal controls and information management systems in place to safeguard its resources and assets, while achieving its mission efficiently and effectively.

DFC plans to dramatically grow its workforce to 700 staff by September 2023. However, DFC faces recruitment challenges. Although DFC is the United States’ development financial institution, it does not offer the higher pay rates of other federal financial institutions, such as the Federal Deposit Insurance Corporation, the Federal Reserve, the Federal Housing Finance Agency, and the National Credit Union Administration. This was a significant concern raised by DFC employees in the 2020 Federal Employee Viewpoint Survey. The OIG intends to assess the extent to which DFC’s pay scale affects its recruitment and retention efforts, and how it compares with other development finance institutions.

The OIG has identified internal control weaknesses through our audit of DFC’s purchase card program and Federal Information Security Modernization Act of 2014 (FISMA) compliance. DFC OIG completed an audit of DFC’s purchase card program, and we found that in some instances DFC failed to retain purchase card records, as defined in the purchase card management plan, and was not compliant with its purchase card and travel card policies, resulting in estimated unsupported questioned costs totaling \$753,087. OIG’s audit of DFC’s compliance with FISMA found that DFC’s information security program and practices were ineffective for FY 2022. The overall maturity level of DFC’s information security program was



“Defined,” essentially a downgrade from our FY 2021 FISMA audit report. The major reason why DFC was downgraded from “Managed and Measurable” (effective) in FY 2021 to “Defined” (ineffective) in FY 2022 was because it did not execute the security practices required by OMB and the Department of Homeland Security.

Managing a transition of DFC to a larger organization while strengthening its internal controls and management systems will continue to be a challenge as DFC grows.



CONCLUSION

In conclusion, DFC has made significant progress in becoming America’s financial development institution; however, as discussed in this report, more work is needed to address the following challenges it faces.

1. *Improving Monitoring and Evaluating Actual Development Impact.*
2. *Improving Performance Management, Transparency, Accuracy, and Availability of Project Data as DFC’s Commitments Grow.*
3. *Balancing Heightened Expectations of Congress and Stakeholders While Managing Risks.*
4. *Managing Organizational Transition While Building Internal Controls Around Core Management Systems.*

This report can be used to share DFC OIG’s work while also helping to inform the debate during discussions with Congress, the Biden Administration, and other stakeholders regarding effective stewardship of U.S. funds dedicated to international financial development. DFC OIG remains committed to conducting thorough and timely audits and investigations of DFC programs and operations, and to recommending actions to help address the issues and challenges we identify. Our goal is to work together with DFC to ensure its success towards its mission, and re-authorization in 2025 in the same bipartisan fashion that DFC was authorized in 2018.



MANAGEMENT'S COMMENTS



DATE: November 14, 2022
TO: Anthony "Tony" Zakel, Inspector General
FROM: Scott Nathan, Chief Executive Officer
SUBJECT: Response to the Inspector General's "Top Management Challenges Facing DFC in FY 2023"

The U.S. International Development Finance Corporation concurs with the four top management challenges identified in the Inspector General's report:

- Improving Monitoring and Evaluating Actual Development Impact.
- Improving Performance Management, Transparency, Accuracy, and Availability of Project Data as DFC's Commitments Grow.
- Balancing Heightened Expectations of Congress and Stakeholders while Managing Risks.
- Managing Organizational Transition while Building Internal Controls around Core Management Systems.

This report underscores the complexity of the many challenges facing DFC and how the independent OIG can bring a fresh perspective to the forefront of agency management. The agency concurs with the list of top challenges but has some concerns with the report's lack of contextualization on how the COVID-19 pandemic impacted on-site monitoring by DFC staff. For instance, the report does not discuss how DFC utilized a variety of alternative tools to ensure that projects continued to be properly monitored during a global health crisis which are important details to fully explain how DFC managed its project monitoring function during this unprecedented time. Since the OIG is positioned to offer DFC management a vital independent lens on the challenges it faces, the OIG's deeper insights and perspectives on the topic are welcomed.

In addition, the report cites actions taken by one of DFC's legacy agencies but the relevance in the context of the agency's current operations is unclear to DFC management as a reader of the report. Rather than automatically adopt the governance structure from either of the legacy agencies, DFC opened for business with an entirely new slate of policies, procedures, and processes that looked to improve on the operations of the legacy agencies. Again, DFC welcomes specific insights from the OIG on how these past challenges from the legacy agencies can be translated into meaningful improvements to the agency's current operating environment.

The level of effort in this report is notable and shows how the OIG's audit processes are helping to strengthen the agency. DFC looks forward to working closely with and learning from the OIG in the coming years.

Sincerely,

Scott Nathan



**Office of Inspector General
U.S. International Development Finance Corporation**

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