OPERATIONAL RISK FRAMEWORK

Differentiated risk-based approach to quality assurance and monitoring, ensuring risks are managed on country-by-country and grant-by-grant basis.
Overall Sector Risk - 65 countries/federal states assessed

- Nearly 75% of countries continue to have medium or low sector risk
- For the 73% countries assessed where the comparison is possible: overall sector risk has slightly decreased across the group with movement in both directions (increase in 6 countries and decrease in 12).
- 1 country/federal state with critical sector risk versus 5 in 2017
Overall Grant Risk - 45 countries/federal states assessed

- 87% of countries rated as low or medium in their overall grant risk
- 1 grant has critical overall grant risk and 5 have high overall grant risk
- Overall grant risk has slightly decreased across the group with movement in both directions (increase in 5 countries and decrease in 5 countries)
The risk matrix covers key risks at the corporate or portfolio level. It includes inherent risk (before mitigation actions), residual risk (current assessment), and target risk (level of acceptable risk).
• Out of 36 risks: 27 have lower residual risk scores than their inherent risk rating; only 6 risks meet their target risk ratings (similar in 2017); 3 residual risk are rated critical.
• **Proposal:** reduce residual risk ratings of 2 risk and increase residual risk ratings of 3 risk.
Proposed changes to the risk matrix

Reduce 2 residual risk ratings:
- Risk 2.2.2: Quality Assurance Process (ESP) => from high to medium (GPC)
- Risk 3.1.4: Liquidity => from medium to low (FRC)

Increase 3 residual risk ratings:
- Risk 4.2.2: Institutional arrangements => from medium to critical (Board)
- Risk 3.1.2: DCP pledges from medium to high (FRC)
- Risk 1.1.7: Foundations Strategy => from medium to high (SIC)
Risk owned by the Board and Risks flagged

Risk owned by the Board:

- Risk 1.1.5: Complementarity/alignment with ECW => residual risk rating medium
- Risk 1.1.6: Complementarity/alignment with IFFEd => residual risk rating critical
- Risk 4.2.2: Secretariat Institutional Arrangement => residual risk rating critical provided proposal from Committees to increase risk rating is approved
- Risk 4.2.3: Secretariat Capacity => residual risk rating high

For the attention of the Board:

- Risk 2.3.3: Program Implementation Modality => residual risk ratings remain critical
- Risk 2.1.4: Co-Financing => addition of a new risk => residual risk rating medium
- Risk 4.2.1: Reputational Risk => residual risk rating remains medium
Objectives
1. Review risk policies/practices to assess gaps and areas for improvement
2. Benchmark current policies/practices against the ones of 3 comparable organizations (GAVI, the Global Fund, the Green Climate Fund)
3. Make recommendations and propose concrete solutions to help the GPE improve its risk assessment methodologies and monitoring of risk mitigation actions
Findings are based on typical Enterprise Risk Management (ERM) Framework

1. Governance and culture

2. Strategy

3. Processes

   Risk Category A (e.g. Operational Risk)

   Risk Category B

   Risk Category C

4. Systems and Infrastructure

   Governance: Oversight structure, risk ownership, roles and responsibilities, risk appetite and culture

   Strategy: Risk management incorporated into strategic decision making

   Risk Processes: Processes for identifying, assessing, controlling/mitigating and reporting/monitoring risks

   Systems and Infrastructure: For supporting ERM framework

Source: Oliver Wyman and IRM
The assessment of GPE’s risk management framework needs to be viewed in the context of its unique institutional set-up and governance.

- **Partnership** (unique organizational structure that creates challenges for both risk management and other governance related issues)
- **Multi-stakeholders** (DCPs, Donors, CSOs, Multilaterals, PS/PF, GAs, CAs, LEGs, etc.)
- **Reliance on third parties on the ground** such as GAs and LEGs (i.e. low performance may lead to GPE not achieving its impact goals as per Strategy 2020)
- **Reliance on Secretariat for administrative and operational support**
- **Secretariat hosted within a larger organization**, and relies on it to provide internal and external audit services (i.e. operational complexity)
- **Board of Directors** (provides support for the objective of the partnership)

These complexities, compared to traditional corporations, create challenges that extend to operational issues and risk management which is what has been explored in this engagement.

*Source: Oliver Wyman*
Confusion around the appropriate allocation of risk management accountability within 3 LoD framework

Current risk management governance and structure

1st line of defense
- Grant Agents, Partnership, LEG, Governments
- Secretariat including country leads
- Board / Committees

2nd line of defense
- Secretariat including country leads
- Board / Committees

3rd line of defense
- World Bank Audit

Strong overlap between 1st and 2nd line roles at the moment which leaves a lot of unclarity around who should be responsible for what and can trigger double work as well as blind spots.

In terms of the third line, GPE does not have its own internal audit function but currently relies on the World Bank’s internal audit function which is not customized to the needs of GPE.

Source: Oliver Wyman
Potential Future 3 LoDs framework

3rd line of defense
World Bank Audit or GPE Internal Audit
- Independently review/test the control framework
- Report to Board, FRC, and Secretariat about the adequacy and effectiveness of control environment

2nd line of defense
Secretariat (Risk team)
- Define control framework
- Monitor risk and controls
- Report/escalate risk or control defects to Mgmt

Country team (CLs)
- Join risk owner-ship of country and sector risk

Committees
- Provide oversight to Secretariat risk functions
- Provide oversight of 1st line of defense

1st line of defense
Grant Agents, Local Education Group, Governments etc.
- Risk ownership of country level risk
- Risk ownership of grant level risks
- Risk ownership of sector risks

Source: Oliver Wyman
Many ERM design choices depend on whether GPE is striving for a centralized or decentralized approach.

<table>
<thead>
<tr>
<th>Decentralized approach</th>
<th>GPE approach</th>
<th>Centralized approach</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Governance</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Heavy Reliance on GAs for 1(^{st}) and 2(^{nd}) Line</td>
<td>• Tendency of GPE Risk Management Team to strive for centralized model and play second line of defense role by challenging and overseeing work performed by first line</td>
<td>• Local grant agents and other third parties perform only first line tasks</td>
</tr>
<tr>
<td>• Secretariat’s role is to provide risk policies but limited challenge and oversight role</td>
<td></td>
<td>• Secretariat staff play strong 2(^{nd}) Line role</td>
</tr>
<tr>
<td>• Strong reliance on third line (audit function)</td>
<td></td>
<td>• Lower importance of third line than decentralized</td>
</tr>
<tr>
<td><strong>Risk Team</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Small Risk Management team</td>
<td>• Too high for decentralized but not high enough for centralized</td>
<td>• Medium Risk Management Team at Secretariat</td>
</tr>
<tr>
<td><strong>Analogues</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><a href="https://www.gavi.org">Gavi</a></td>
<td><a href="https://www.gppnet.org">GLOBAL PARTNERSHIP FOR EDUCATION</a></td>
<td><a href="https://www.theglobalfund.org">TheGlobalFund</a></td>
</tr>
<tr>
<td><strong>Considerations</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Fewer FTE costs</td>
<td>• Higher FTE costs</td>
<td></td>
</tr>
<tr>
<td>• Less direct control over risk management,</td>
<td>• More direct control</td>
<td></td>
</tr>
<tr>
<td>• Analogues focus on delivery of goods</td>
<td>• Analogues focus on delivery of services and support direct giving</td>
<td></td>
</tr>
</tbody>
</table>
Six Key Findings

1. Risk appetite statement
2. Risk governance
3. Incorporation of risk into business decisions & strategic planning
4. Risk taxonomy
5. Monitoring & Reporting
6. Framework and policy documents

Source: Oliver Wyman
FRC Considerations

- Need for **user friendly risk taxonomy** as part of the recommendations in the review.
- On centralized vs. decentralized approach: there might be a **blended** approach that relates to **GPE’s uniqueness** as a partnership.
- **Roles and Responsibilities should be clarified at the 1st and 2nd levels of the 3 lines of defense model** to prevent overlaps and blind spots.
- Implementation of mitigation actions is mostly focused on the Secretariat while it should **involve all the stakeholders**.
- Need to establish a **risk tolerance/appetite for each risk partnership-wide**.
Overarching findings and recommendations of Effective Partnership Review reinforce the Risk Review

Roles & responsibilities: clear on paper, ambiguity in practice

Reinforce the risk review report:

“Simplification of the governance structure and the associated roles and responsibilities will remediate many gaps” (Oliver Wyman)

Source: Oliver Wyman and Effective and Efficient Partnership Study
Secretariat proposed workplan

Step 1: Review risk taxonomy

**What:** Mapping of risk framework components

**Deliverable:** Final taxonomy

**Timeline:** FRC and Board meetings Fall 2018

Step 2: Develop risk appetite statements

**Deliverable:** Risk appetite statement within updated risk taxonomy

**Timeline:** FRC and Board meetings Fall 2018

Step 3: Review 3 LoD model

**What:** Clarify 1st and 2nd LoD. To be dealt in conjunction with next steps on the Effective Partnership Review

**Timeline:** FRC and Board meetings Spring 2019

Step 4: Define KRI and KCI

**What:** Based on the 3 LoD model (i.e. 1st LoD are risk owners and provide inputs for KRI and KCI)

**Timeline:** FRC and Board meetings Spring 2019
BOD/2018/16-XX—Risk Management Report: The Board of Directors:

1. Endorses the changes to the Risk Matrix, including update on current mitigations actions and addition of future mitigation actions, revisions to the overall score of some risks, and update on risk wording, as presented in BOD/2018/6 DOC 13.

2. Requests the Secretariat to commence implementation of the recommendations arising from the external review of risk management based on existing resources and capacity and to report to the FRC on progress at its next meeting.
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### Potential roles and responsibilities across risk management (for discussion)

<table>
<thead>
<tr>
<th>Description</th>
<th>Owner</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Risk Mgmt Strategy</strong></td>
<td></td>
</tr>
<tr>
<td>• Risk appetite</td>
<td>Board</td>
</tr>
<tr>
<td>• Risk management principles</td>
<td>FRC</td>
</tr>
<tr>
<td><strong>Risk Mgmt Process</strong></td>
<td></td>
</tr>
<tr>
<td>• Process to implement risk strategy</td>
<td>Secretariat Committees</td>
</tr>
<tr>
<td><strong>Identification</strong></td>
<td></td>
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<tr>
<td>• Identify threats, cause of losses/malfunctions</td>
<td>1st line</td>
</tr>
<tr>
<td><strong>Notification</strong></td>
<td></td>
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<tr>
<td>• Regularly inform GRM the risks identified</td>
<td>1st line</td>
</tr>
<tr>
<td><strong>Assessment</strong></td>
<td></td>
</tr>
<tr>
<td>• Assess risks in both quantitative and qualitative manner</td>
<td>Secretariat</td>
</tr>
<tr>
<td><strong>Control</strong></td>
<td></td>
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<tr>
<td>• Risk control to minimize risk</td>
<td>1st line</td>
</tr>
<tr>
<td><strong>Reporting</strong></td>
<td></td>
</tr>
<tr>
<td>• Board is informed of material risks’ assessment and countermeasure</td>
<td>Secretariat</td>
</tr>
</tbody>
</table>