

PROJECT FINANCIAL MANAGEMENT ASSESSMENT

EXECUTIVE SUMMARY

Overall Assessment

1. Without mitigating measures, the financial management risk was assessed as substantial, due to some capacity gaps in the staff and asset management procedures at the Ministry of Education, Culture, Science and Sports (MECSS). With mitigating measures in place, the project risk would be reduced to moderate. The capacity gaps in internal controls and the internal audit function identified in the previous assessment¹ have been improved with the recruitment of two additional internal auditors and an effort to strengthen the internal audit function at the MECSS. However, the internal auditors have not yet begun producing a significant number of audits. Therefore, the internal audit function at the MECSS still needs improvement. The risk mitigation measures adopted for previous projects have been effective and similar measures should be adopted for this project. In general, the risks can be mitigated by establishing a qualified project implementation unit (PIU) with a project coordinator and financial management specialist and/or accountant and developing strong internal controls for managing project funds and assets. Though these measures did not permanently address the challenges at the MECSS, they were effective in providing the necessary capacity in the PIU for previous projects. Therefore, this project should address those risks in the same way—building the capacity of the MECSS in project management, asset management, and of the newly established Internal Audit Committee.

Summary of Weaknesses and Risks Identified

2. The MECSS financial management staff have limited experience with managing donor funded projects. Although the MECSS has implemented and is currently implementing a number of the Asian Development Bank (ADB)-financed projects, they have been and are being managed by separate PIUs established by the MECSS and staffed with consultants, including qualified financial management specialists and/or accountants, to provide the necessary financial management capacity. Also, the government financial management information system (GFMIS), a software being used by the Government of Mongolia, including the MECSS, does not have the capacity to manage donor funded projects. Some weaknesses are found in the internal controls in the area of asset management. Specifically, the procedure to verify goods received and the control of assets once in circulation should be strengthened. The weaknesses previously identified in the internal audit function have been addressed to some extent (i.e., renaming and strengthening of the department and recruiting two additional internal auditors to make the total number of internal auditors four), but the Monitoring, Evaluation and Internal Audit Department of the MECSS has not yet started to conduct regular audits to test and improve internal controls in sufficient volume to be effective. They also have limited knowledge and experience of ADB requirements and projects. Nonetheless, the audit of this project has been included in the department's work plan.

Summary of Mitigation and/or Management Measures to be Adopted

3. The MECSS will select and recruit a financial management specialist and/or accountant to the PIU in consultation with ADB. The terms of reference (TOR) for the financial management

¹ Asian Development Bank. 2015. *Project Financial Management Assessment Report* (Supplementary Linked Document to the Report and Recommendation of the President for Improving School Dormitory Environment for Primary Students in Western Region Project). Manila.

specialist and/or accountant will be reviewed and approved by ADB which will also review and provide guidance in the selection and recruitment processes. This will mitigate the risk associated with the lack of project management experience on the part of the MECSS financial management staff. The PIU financial management specialist and/or accountant should receive training on ADB disbursement. To mitigate the risks arising from managing the project outside the GFMIS, an accounting software acceptable to ADB will be installed at the PIU to manage the project funds. The accounting software can also mitigate asset management risks as basic asset data can be stored by using the software. Project assets will be tracked and labeled and reported in project quarterly and annual reports. During review missions, ADB will review transactions and financial reports. The MECSS staff will also be trained in ADB's guidelines and procedures so that the risks associated with weaknesses in the internal audit function and lack of direct project management experience at the MECSS shall be mitigated.

I. INTRODUCTION

4. In accordance with ADB's *Guidelines for the Financial Management and Analysis of Projects*, the *Financial Due Diligence: A Methodology Note*, and the *Financial Management Technical Guidance Note: Financial Management Assessment*, the financial management assessment (FMA) was conducted on 13 February–21 March 2017. The FMA considered the capacity of the MECSS (the executing and implementing agency of the project), including funds flow arrangements, staffing, accounting and financial reporting systems, financial information systems, and internal and external auditing arrangements. Other public financial management assessment reports were also reviewed during the FMA.² Preparation activities included reviewing documents and ADB's ongoing experience, interviews with counterparts, and discussions with stakeholders. The Financial Management, Internal Control and Risk Assessment was conducted by financial experts Michael Halbert and Battsagaan Jantsankhorloo.

II. BRIEF PROJECT DESCRIPTION

5. The government of Mongolia requested ADB's support against a background of serious economic difficulties which have led to large revenue shortfalls and cuts in government budget, including that for the education sector. The project aims to sustain access to and quality of education during economic difficulties through the following five outputs: (i) gap in enrollment capacity of schools and kindergartens narrowed; (ii) unfinished curriculum reform and associated assessment system reforms completed; (iii) teaching and learning materials that accompany the new curriculum provided; (iv) teachers' and managers' knowledge and skills upgraded for the new curriculum and assessments; and (v) systems for planning and managing education services strengthened. The project is estimated to cost \$50.69 million and will finance civil works, school equipment and furniture, teaching-learning materials, tools and equipment, training, workshops, project management, physical and price contingencies, interest, and other charges during implementation. The project will be implemented from November 2017 to June 2021. The executing agency of the project will be the MECSS. The implementing agencies will be the MECSS and Ulaanbaatar Metropolitan Education Department.

III. COUNTRY AND SECTOR FINANCIAL MANAGEMENT ISSUES

6. The country-specific risks have been assessed as moderate because of the need to manage donor projects and funds outside GFMIS, weak budget credibility, some non-competitive

² International Monetary Fund. 2011. *IMF Country Report No. 11/107 Mongolia: Financial System Stability Assessment*. Washington, D.C.; World Bank. 2015. *Mongolia Public Financial Management Performance Report*. Washington, D.C.

procurement practices, and weaknesses in some areas of control in the GFMIS.³ The entity-specific risks were assessed as substantial due to limited experience of the MECSS staff in directly managing donor funds, some weakness in managing and controlling fixed assets, and the internal audit unit that is not yet fully functional. The MECSS has a good record of preparing credible budgets and has not made significant budget adjustments during the execution stage in recent years.

IV. PROJECT FINANCIAL MANAGEMENT SYSTEM

A. Overview

(i) Organization and Staff Capacity

7. The MECSS is a government agency established by the resolution of the State Great Khural (Parliament) under the Government Resolution No.7 dated 27 May 2016. There are three main laws governing its financial management: (i) the Accounts Law, (ii) the Budget Law, and (iii) the Law on Transparency of Information and the Right to Receive Information. It was found that the MECSS has procedures, staff, and internal controls in place to ensure compliance with the mentioned regulations and the interviewed staff are adequately trained.

8. The MECSS's senior management is comprised of the minister; vice minister; state secretary; and eight directors of Education Policy Department, Science and Technology Policy Department, Culture Policy Department, Sport Policy Department, Administration Department, Policy Implementation Department, Finance and Economics Department, and Monitoring, Evaluation and Internal Audit Department. The MECSS's organizational and governance structure is appropriate for the project.

9. The MECSS Finance and Economics Department has 17 staff including the department head, a chief accountant, and three more officers responsible for accounting, reporting and treasury, as well as five staff responsible for various components of the budget. Its investment division, which will be supporting the project implementation, has six staff. The MECSS will select and recruit a financial management specialist and/or accountant to the PIU which will manage project funds and prepare financial reports. There will also be a project coordinator to ensure the project is managed effectively as per government regulations and ADB requirements.

(ii) Information Management

10. Like all government agencies in Mongolia, the MECSS uses the GFMIS software to track data and prepare reports. However, donor funds are managed outside the GFMIS. Annual and quarterly financial reports for submission to the Ministry of Finance (MOF), are formatted outside the system using the GFMIS data. The GFMIS is password protected and backed up by the MOF. The MECSS has adequate systems and procedures to safeguard and store documents and electronic data. The PIU will need to acquire a basic accounting software and to set up storage and backup systems for documents and electronic data.

(iii) Budgeting and Funds Flow Arrangements

11. The MECSS's budgets are prepared in accordance with the MOF requirements. Drafts are prepared by the Department of Finance and Economics in collaboration with department

³ World Bank. 2015. *Mongolia Public Financial Management Performance Report*. Washington, D.C.

heads and other staff and approved by the MECSS's management and the minister. They are prepared using the government standard chart of accounts and economic classifications. The MOF approved the budget and prepares the consolidated budget for the entire government and submits them for approval to the State Great Khural. The MECSS's budgets include performance and financial targets. Budget execution is controlled by the GFMIS which does not allow expenses to be processed unless there is sufficient budget and monthly reports are prepared for management. As required, reports are also prepared for the MOF which include budget versus actual comparisons and descriptions of any budget adjustments. Budget adjustments can be requested by the MECSS in advance within limits as prescribed by the MOF but in recent years the MECSS has not had to request an inordinate amount of budget adjustments.

(iv) Effectiveness

12. The country's public financial management system is governed by three laws: (i) the Accounts Law, (ii) the Budget Law, and (iii) the Law on Transparency of Information and the Right to Receive Information. Budget preparation is based on a medium-term (3-year) planning framework and the MECSS has several staff devoted to budget preparation and management. The MECSS has been preparing adequate budgets that have been well planned with only moderate adjustments required during execution. The MECSS, like all ministries, uses the GFMIS software which incorporates several internal controls which reduces risks of over spending budget lines. The GFMIS makes financial reporting accurate and timely although reports need to be formatted outside the system. The Monitoring, Evaluation and Internal Audit Department was established in a government-wide reorganization exercise in 2015. Now, there are nine staff including the director and four internal auditors as opposed to two in 2015 when the previous FMA was conducted. All the internal auditors are well qualified but they have not been active in conducting audits and have only produced a few audits. On 13 March 2017, the Internal Audit Committee has been established within the MECSS with the Ministry Order No. A/83. The committee is comprised of nine members and headed by the Minister of MECSS. The committee meets quarterly to discuss planning, monitoring, reporting with the ministry, and its functions. Yet, the overall internal audit function remains weak. The National Audit Office performs audit of financial statements submitted by the government and reports to the State Great Khural.

(v) Accountability Measures

13. The government of Mongolia is required to submit annual financial statements 6 weeks after the fiscal year end to the State Great Khural and the National Audit Office for external audit. The reports must also include budget versus actual executed budget, data and other information required by the various laws governing financial management of state entities in Mongolia. Moreover, in accordance with the Law of Mongolia on Glass Accounts (approved in July 2014 and effective in January 2015), all government agencies and legal entities with state involvement are required to make information on budgets and financial matters, including the utilization of financing and other government indebtedness, available to the public. The MECSS's bi-annual and annual financial statements are published on their website (www.mecss.gov.mn) as well as integrated government platform for financial reporting (<http://shilendans.gov.mn/>). The Monitoring, Evaluation and Internal Audit Department is responsible for ensuring internal controls and compliance with regulations, policies, and procedures.

B. Strengths

14. A PIU will be established by the MECSS and staffed with qualified professionals, including a project coordinator and financial management specialist and/or accountant. They will develop procedures to ensure compliance with legislation and ADB requirements. The PIU and key MECSS staff will be trained in ADB procedures and requirements. Annual budgets and quarterly and annual reports of the project will be reviewed and approved by a project steering committee to be established by the MECSS. The loan proceeds will be disbursed in compliance with ADB's *Loan Disbursement Handbook* (2017, as amended from time to time). Direct payment by ADB, and imprest fund procedures, liquidation and replenishment, and statement of expenditures, will be used to disburse the loan proceeds. An imprest account will be established at the State Bank of Mongolia, while a sub-(operational) account will be established at a well-established commercial bank. The PIU will acquire a basic accounting software to manage the projects funds. The system will securely store financial data and will directly generate financial reports.

C. Weaknesses

15. The MECSS has limited experience in directly managing donor funds, as donor funds have been managed outside the government system. The MECSS will select and recruit a financial management specialist and/or accountant to the PIU. There is risk that a qualified and experienced financial management specialist/accountant may not be recruited to the PIU, which will be mitigated through ADB's involvement in all stages of recruitment, from developing the TORs and prior review of selection reports. The asset management and goods receipt procedures will need to be strengthened. Assets are recorded and tracked in the GFMS when purchased. However, there are limited systems and procedures to track assets once in circulation, including details about who is in possession of an asset. Physical audits against the GFMS records are conducted regularly. The MECSS's Department of Monitoring and Evaluation and Internal Audit has recently been strengthened with four internal auditors. Yet they have only produced a few audits and are not fully functional. The internal auditors also have limited experience and understanding of ADB's guidelines and procedures.

D. Personnel, accounting policies and procedures, internal control, internal and external audit

16. The PIU will be established by the MECSS to manage the project, including financial management. The PIU will be staffed by qualified and experienced professionals including a project coordinator responsible for the overall project management, a financial management specialist and/or accountant, a procurement specialist, and a monitoring and evaluation specialist. The financial management specialist and/or accountant and key MECSS staff will be trained in ADB disbursement. Internal policies and procedures at the MECSS will be improved to strengthen internal controls over assets and ensure ADB requirements are met. The Internal Audit Committee will be provided with training and an internal audit charter will be developed. The government accounting system and chart of accounts will be used and accounting software, acceptable to ADB, to be installed at the PIU. Policies and procedures will be established by the PIU at the beginning of project to ensure compliance with regulations and ADB requirements. Project assets will be tracked in the accounting software and labeled. Their use will be reported in project quarterly and annual reports. Annual budgets and quarterly and annual reports will be reviewed and approved by the project steering committee. ADB will conduct missions to review financial transactions, reports, and records. An external auditor acceptable to ADB will be appointed by the National Audit Office for the project. TOR for the external auditor will be prepared by the National Audit Office and approved by ADB.

E. Financial reporting systems, including use of information technology

17. An accounting software system will be installed at the PIU. The system will directly generate financial reports. The PIU will set up a project performance management system to track and report progress. The PIU will prepare quarterly and annual reports on financial and project progress as per government and ADB requirements.

F. Disbursement arrangements, funds flow mechanism

18. Civil works contractors and other large suppliers will be paid directly by ADB. Operational expenses will be paid from an imprest fund set up by the PIU, on behalf of the MECSS. The imprest funds will be held at the State Bank of Mongolia and a sub-account, in well-established bank. ADB procedures will be followed and the PIU financial management specialist and/or accountant will be trained in ADB procedures. The funds flow diagram is in Appendix 2.

V. RISK DESCRIPTION AND RATING—INCLUDING THE FINANCIAL MANAGEMENT AND INTERNAL CONTROL RISK ASSESSMENT

Risk Type	Risk Assessment	Risk Description	Mitigation Measures or Risk Management Plan
Inherent Risk			
1. Country-Specific Risks	Moderate	<p>The government of Mongolia including the Ministry of Education, Culture and Science and Sports (MECSS) uses a financial management software known as GFMIS, government financial management information system. This is a centralized system operated by the Ministry of Finance.</p> <p>The MECSS staff report that the GFMIS system store budget and actual expenditure data effectively and supports their financial management needs including budget control and financial reporting. However, the system currently does not have the capacity to manage donor funds and projects.</p>	<p>The MECSS Finance and Economics Department will be assisted by the project implementation unit (PIU) in preparing annual budgets and plans for the project in accordance with the design and monitoring framework, the project administration manual and loan agreement.</p> <p>The PIU will acquire an accounting software to manage the projects funds.</p>
2. Entity-Specific Risks	Substantial	While the MECSS has implemented ADB and other donor-funded projects, donor funds are managed outside the GFMIS system. A PIU has been established and staffed by professionals, including a	A PIU will be established by the MECSS to manage the project, including financial management. The PIU will be staffed by qualified and experienced professionals including a project coordinator responsible for the

Risk Type	Risk Assessment	Risk Description	Mitigation Measures or Risk Management Plan
		<p>financial management specialist and/or accountant to manage donor-funded projects. The MECSS staff themselves have limited experience in directly managing financial aspects of donor funded projects. Hence, they currently do not have the capacity to manage donor funds in compliance with ADB requirements.</p> <p>Internal audit at the MECSS is the responsibility of the Monitoring, Evaluation and Internal Audit Department. The department has been created in 2015 and is now capable of providing adequate internal audit function of the MECSS as they have four well-qualified internal auditors. This is an improvement since the assessment conducted in 2015. However, they have not yet begun to conduct and produce a significant number of audits.</p> <p>The procedures concerning controlling assets could be improved, and especially in the receipt of goods. Currently, the Investment Officer who organized the procurement is the only person checking goods received. A procurement professional or other officer should also check goods received and certify that the goods match the invoice and purchase order.</p>	<p>overall project management, and a financial management specialist and/or accountant to manage the project funds. A project steering committee will be established by the MECSS to oversee the project. Policies and procedures will be developed to ensure compliance with regulatory and ADB requirements.</p> <p>The system to control and track project assets will be improved and assets will be labeled. The Head of Monitoring, Evaluation and Internal Audit Department has agreed to provide internal audit support to the project further ensuring effective internal controls over project assets, information and reports, and compliance with ADB requirements.</p>
Overall Inherent Risk	Substantial		
Project Risk			
1. Implementing Entity	Low	The MECSS financial management system is governed by various laws and regulations. The MECSS's	The MECSS will establish a PIU which will include a financial management specialist and/or accountant to manage the

Risk Type	Risk Assessment	Risk Description	Mitigation Measures or Risk Management Plan
		organizational and management structures are adequate for the financial management of the project. However, they do not have any staff with donor project management experience other than PIUs of existing projects.	project funds. There will also be a project steering committee to oversee the project, review reports, and recommend improvements.
2. Funds Flow	Low	The funds flow arrangements currently used by the MECSS for ADB projects will be used for the project. The PIU will request and monitor direct payments, manage the imprest fund, and follow the statement of expenditure (SOE) procedures.	A PIU will be established by the MECSS and will include a project coordinator and a financial management specialist/accountant who should have experience with ADB or similar projects. Loan proceeds will be disbursed in compliance with ADB's <i>Loan Disbursement Handbook</i> (2017, as amended from time to time). Direct payments to contractors and suppliers by ADB, an imprest fund procedures, liquidation and replenishment, and SOEs will be used to disburse the loan proceeds. The imprest account will be established at the State Bank of Mongolia and a sub account will be established at a well-established commercial bank acceptable to ADB.
3. Staffing	Substantial	The MECSS will recruit a financial management specialist and/or accountant for the PIU. The current staff at the MECSS do not have the capacity to manage donor funded projects.	Terms of reference (TOR) for the financial management specialist and/or accountant will be reviewed and approved by ADB, as well as the selection and recruitment processes. A qualified project coordinator should oversee the work of the financial management specialist and/or accountant other key staff should be provided with training in ADB requirements. The MECSS staff will also be trained in ADB guidelines and policies.
4. Accounting Policies and Procedures	Substantial	The MECSS uses the government accounting system which meets international accounting standards. The government regulations governing fixed asset	The PIU will utilize the government accounting system, chart of accounts, International Public Sector Accounting Standards, and an accounting software. Accounting policies

Risk Type	Risk Assessment	Risk Description	Mitigation Measures or Risk Management Plan
		accounting exist but no procedures are in place to adequately safeguard assets.	and procedure manuals will be compiled by the PIU to comply with regulatory and ADB requirements for financial reporting and internal control activities, including control of assets and contracts.
5. Internal Audit	Low	The Monitoring, Evaluation and Internal Audit Department has been established in 2015 and there are four qualified internal auditors in the department. To date they have not yet conducted a significant number of audits but they do plan to audit the project.	The MECSS staff will be trained in ADB's guidelines and procedures. The MECSS internal auditors will also audit the project. The ADB will conduct missions to review transactions and financial reports.
6. External Audit	Low	Annual external audits are conducted by the National Audit Office in accordance with the International Standards on Auditing. The audit reports of the MECSS for the past 3 years identified no major issues, though interviews with the MECSS staff revealed that there were some issues with funds and resources misused, which were nevertheless all addressed. The National Audit Office has knowledge and understanding of ADB's guidelines and procedures.	An external auditor will be appointed by the National Audit Office for the project and approved by the ADB. TOR for the external auditor will be prepared by the National Audit Office and approved by ADB.
7. Reporting and Monitoring	Low	The MECSS prepares final quarterly and annual financial reports outside of GFMS but using GFMS data. The MECSS prepares quarterly and annual financial reports on time generally and they have had mainly positive audits of previous annual financial statements.	An accounting software will be used by the PIU and linked to the project performance monitoring system. The system will directly generate financial reports. The PIU will prepare quarterly and annual reports on financial and physical progress in project implementation.
8. Information Systems	Low	The MECSS uses the government GFMS accounting software. Final annual and quarterly financial reports are prepared outside of GFMS using GFMS data. Donor funds are managed outside the government system.	The PIU will purchase accounting software to track and securely store data. The software will produce financial reports in the required format directly from the system. The PIU will develop procedures to securely store documents and electronic data.

Risk Type	Risk Assessment	Risk Description	Mitigation Measures or Risk Management Plan
Overall Project Risk	Moderate		
Overall (Combined) Risk	Moderate		

VI. PROPOSED TIME-BOUND ACTION PLAN

19. The following actions will be taken to minimize the key risks identified above.

Key Risks	Activity to Mitigate Risks	Staff/Personnel Responsible	Timeline
Limited capacity and experience of the MECSS staff in managing donor funds	Establish a PIU with a project coordinator and financial management specialist and/or accountant with experience in managing ADB or similar projects and the necessary skills and experience. Train MECSS and PIU staff on ADB disbursement.	MECSS	Immediately after loan effectiveness
	Approve TORs for the PIU and oversee the process.	ADB	Before and after loan effectiveness
	In addition to the project administration manual, develop detailed accounting procedures to ensure effective management and control of the project funds and assets.	PIU staff	Immediately after loan effectiveness
Donor funds are managed outside the GFMS system	Utilize the government accounting systems and chart of accounts, (IPSAS standards) and procure an accounting software for the PIU.	PIU staff	Immediately after loan effectiveness
Some issues with asset management and goods receipt procedures	Develop procedures to ensure proper control of project assets which will be overseen by the PIU. Track assets in the accounting software for the PIU.	PIU staff	Immediately after loan effectiveness
Not yet fully functioning internal audit function	Provide training for the Internal Audit Committee and develop an internal audit charter. Ensure procedures are developed to comply with regulatory and ADB requirements. Train MECSS and PIU staff in ADB's guidelines and procedures. Conduct review missions regularly.	ADB, MECSS	Periodically as required

ADB = Asian Development Bank; GFMS = government financial management information system; MECSS = Ministry of Education, Culture, Science and Sports; PIU = project implementing unit, TOR = terms of reference.

VII. SUGGESTED FINANCIAL MANAGEMENT COVENANTS

20. The standard assurances would suffice, given the overall project risk was assessed as moderate.

VIII. CONCLUSION

21. The MECSS has adequate systems and staff in place but they will need a PIU with a qualified staff to manage the project. The TORs of the staff and their recruitment will be approved by ADB. The project steering committee and ADB will also monitor the project.

APPENDICES:

1. Completed Financial Management Assessment Questionnaire
2. Funds Flow Diagram

APPENDIX 1: FINANCIAL MANAGEMENT ASSESSMENT QUESTIONNAIRE

Topic	Response	Potential Risk Event
1. Executing / Implementing Agency		
1.1 What is the entity's legal status / registration?	The Ministry of Education, Culture, Science and Sports (MECSS), will be the executing and implementing agency of the project. It is a Government of Mongolia ministry established by the resolution of the State Great Khural (Parliament).	Low
1.2 How much equity (shareholding) is owned by the Government?	The MECSS is a government agency.	Low
1.3 Obtain the list of beneficial owners of major blocks of shares (nongovernmental portion), if any.	Not applicable.	Low
1.4 Has the entity implemented an externally-financed project in the past? If yes, please provide details.	The MECSS has implemented several externally financed projects, including: The Global Partnership for Education Preschool Education Project (GPE/World Bank, 2013–2016); Higher Education Reform Project (ADB, 2011–2015); Education for the Poor–Financial Crisis Response Project (ADB, 2009–2014); Education Sector Reform Project (ADB, (2008–2014); Skills for Employment (ADB 2013-) and Improving School Dormitory (ADB 2015-)	Low

Topic	Response	Potential Risk Event
1.5 Briefly describe the statutory reporting requirements for the entity.	There are three laws with reporting requirements that the MECSS must comply with, the Accounts Law, the Budget Law, and the Law on Transparency of Information and the Right to Receive Information of Mongolia.	Low
1.6 Describe the regulatory or supervisory agency of the entity.	The MOF, the National Audit Office, and the State Great Khural (Parliament) oversee the MECSS.	Low
1.7 What is the governing body for the project? Is the governing body for the project independent?	The project will have a project steering committee organized by the MECSS but will also include representatives from MOF, Ulaanbaatar Metropolitan Education Department, Engineering Supply Department of Ulaanbaatar Municipality, Education Evaluation Center, Institute for Teachers' Professional Development, and Institute of Education	Low
1.8 Obtain current organizational structure and describe key management personnel. Is the organizational structure and governance appropriate for the needs of the project?	<p>The MECSS's management positions comprise: 1 minister; 1 vice minister; 1 state secretary; 8 department directors Education Policy, Science and Technology Policy, Culture Policy, Sport Policy, Administration, Policy Implementation, Finance and Economics and Monitoring, Evaluation and Internal Audit.</p> <p>The MECSS's organizational and governance structure is adequate to support the project.</p>	Low
1.9 Does the entity have a Code of Ethics in place?	The Government Resolution No.58 (1999) set up the Code of Conduct for all Public Administrative Officials.	Low
1.10 Describe (if any) any historical issues report of ethics violations involving the entity and management. How were they addressed?	There have been no significant issues in the last 3 years.	Moderate
2. Funds Flow Arrangements		
2.1 Describe the (proposed) project funds flow arrangements in detail, including a funds flow diagram and explanation of the flow of funds from ADB, government and other financiers, to the government, EA, IA, suppliers, contractors, ultimate beneficiaries, etc. as applicable.	Large payments to civil works contractors and other vendors will be paid directly by ADB. Smaller local suppliers and contractors, PIU operational expenses and items such as training and workshops, will be paid using imprest accounts to be opened by the PIU. The ADB will fund the imprest account.	Low

Topic	Response	Potential Risk Event
2.2 Are the (proposed) arrangements to transfer the proceeds of the loan (from the government / Finance Ministry) to the entity and to the end-recipients satisfactory?	Yes. the PIU Financial management specialist/accountant will control all payments and receipts as well as the imprest account. Larger payments will be made directly by the ADB upon receipt of adequate supporting documents.	Low
2.3 Are the disbursement methods appropriate?	The disbursement methods are in compliance with ADB's guidelines.	Low
2.4 What have been the major problems in the past involving the receipt, accounting and/or administration of funds by the entity?	No significant issues in the last three years.	Low
2.5 In which bank will the Imprest Account (if applicable) be established?	Imprest accounts will be established at a commercial bank approved by ADB.	Low
2.6 Is the bank in which the imprest account is established capable of –(i) Executing foreign and local currency transactions? (ii) Issuing and administering letters of credit (LC)? (iii) Handling a large volume of transaction? (iv) Issuing detailed monthly bank statements promptly?	The bank selected will be a large well established bank with a proven capability to do all of these.	Low
2.7 Is the ceiling for disbursements from the imprest account and SOE appropriate/required?	The amount requested to fund the imprest account will be based on forecasted ADB financed expenditures to be paid from the imprest account 6 months in advance.	Low
2.8 Does the (proposed) project implementing unit (PIU) have experience in the management of disbursements from ADB?	The PIU will be established once the loan becomes effective. Staff who have experience with ADB-financed projects will be selected as PIU staff, if possible.	Substantial
2.9 Does the PIU have adequate administrative and accounting capacity to manage the imprest fund and statement of expenditure (SOE) procedures in accordance with ADB's Loan Disbursement Handbook (LDH)? Identify any concern or uncertainty about the PIU's administrative and accounting capability which would support the establishment of a ceiling on the use of the SOE procedure.	Staff who have experience with ADB projects will be selected for the PIU if possible. The PIU will be established before the loan becomes effective.	Substantial
2.10 Is the entity exposed to foreign exchange risk? If yes, describe the entity's policy and arrangements for managing foreign exchange risk.	The MECSS has no exchange risk as they only deal in local currency.	Low

Topic	Response	Potential Risk Event
2.11 How are the counterpart funds accessed?	The details of the counterpart contributions have not yet been determined but they will likely be “in kind” contributions which will be tracked and recorded by the PIU.	Low
2.12 How are payments made from the counterpart funds?	They will probably be “in kind” contributions.	Low
2.13 If project funds will flow to communities or NGOs, does the PIU have the necessary reporting and monitoring arrangements and features built into its systems to track the use of project proceeds by such entities?	No project funds will flow to communities or NGOs.	Low
2.14 Are the beneficiaries required to contribute to project costs? If beneficiaries have an option to contribute in kind (in the form of labor or material), are proper guidelines and arrangements formulated to record and value the labor or material contributions at appraisal and during implementation?	Not applicable.	Low
3. Staffing		
3.1 What is the current and/or proposed organizational structure of the accounting department? Attach an organization chart.	The Finance and Economics Department of the MECSS has an Investment Division with a Division Head and five officers in-charge of different types of investments. There are five budget officers including a senior officer and five staff with different accounting functions. The senior budget officer is responsible for donor project budgets.	Low
3.2 Will existing staff be assigned to the project, or will new staff be recruited?	A financial management specialist/accountant will be recruited for the PIU as current staff do not have significant capacity in managing donor projects/funds.	Substantial
3.3 Describe the existing or proposed project accounting staff, including job title, responsibilities, educational background and professional experience. Attach job descriptions and CVs of key existing accounting staff.	Financial management specialist/accountant will be included on the PIU. They should be an accounting professional who has experience in financial management of ADB projects or similar. The TOR for the accountant/financial management specialist will be reviewed and approved by ADB.	Substantial
3.4 Is the project finance and accounting function staffed adequately?	The PIU will be staffed by a financial management specialist/accountant with the necessary skills and experience.	Substantial

Topic	Response	Potential Risk Event
3.5 Are the project finance and accounting staff adequately qualified and experienced?	The financial management specialist/accountant should be an accounting professional who has experience in financial management of ADB projects. The TOR for the financial management specialist/accountant specialist and selection will be approved by ADB.	Substantial
3.6 Are the project finance and accounting staff trained in ADB procedures, including the disbursement guidelines (i.e., LDH)?	The financial management specialist/accountant should be qualified but training in ADB procedures will also be provided.	Substantial
3.7 What is the duration of the contract with the project finance and accounting staff?	The financial management specialist/accountant will be contracted for the life of the project throughout implementation and close out.	Low
3.8 Identify any key positions of project finance and accounting staff not contracted or filled yet, and the estimated date of appointment.	The financial management specialist/accountant will be recruited as soon as it is practical.	Substantial
3.9 For new staff, describe the proposed project finance and accounting staff, including job title, responsibilities, educational background and professional experience. Attach job descriptions.	The financial management specialist/accountant for the PIU will be an accounting professional who has experience in financial management of ADB or similar projects. The TOR for the financial management specialist/accountant will be approved by ADB.	Low
3.10 Does the project have written position descriptions that clearly define duties, responsibilities, lines of supervision, and limits of authority for all of the officers, managers, and staff?	The TORs for the PIU staff will clearly outline their tasks, responsibilities, and levels of authority. The TORs will be reviewed and approved by ADB.	Low
3.11 What is the turnover rate for finance and accounting personnel (including terminations, resignations, transfers, etc.)?	There has not been significant turnover rate for the financial management specialist/accountants under previous ADB projects implemented by MECSS	Low
3.12 What is training policy for the finance and accounting staff?	The financial management specialist/accountant will be given training in ADB procedures and requirements.	Low
3.13 Describe the list of training programs attended by finance and accounting staff in the last 3 years.	The MECSS staff have attended numerous training but not in the area of project financial management.	Low
4. Accounting Policies and Procedures		

Topic	Response	Potential Risk Event
4.1 Does the entity have an accounting system that allows for the proper recording of project financial transactions, including the allocation of expenditures in accordance with the respective components, disbursement categories, and sources of funds (in particular, the legal agreements with ADB)? Will the project use the entity accounting system? If not, what accounting system will be used for the project?	The MECSS uses the Government of Mongolia's GFMIS software which effectively stores and tracks all financial data. However, it does not have the capacity to manage donor projects, so a basic accounting software should be purchased.	Low
4.2 Are controls in place concerning the preparation and approval of transactions, ensuring that all transactions are correctly made and adequately explained?	Procedures to ensure effective internal controls for the project funds will be established. Transactions will be prepared by the PIU financial management specialist/accountant approved by the MECSS, the MOF, and ADB as required.	Low
4.3 Is the chart of accounts adequate to properly account for and report on project activities and disbursement categories? Obtain a copy of the chart of accounts.	The chart of accounts for the MECSS is the Government of Mongolia standard chart of accounts and is adequate for the project.	Low
4.4 Are cost allocations to the various funding sources made accurately and in accordance with established agreements?	Yes.	Low
4.5 Are the General Ledger and subsidiary ledgers reconciled monthly? Are actions taken to resolve reconciliation differences?	Yes, they are reconciled monthly and there are procedures to review the reconciliations and ensure errors are corrected.	Low
4.6 Describe the EA's policy for retention of accounting records including supporting documents (e.g., ADB's policy requires that all documents should be retained for at least 1 year after ADB receives the audited project financial statements for the final accounting period of implementation, or 2 years after the loan closing date, whichever is later). Are all accounting and supporting documents retained in a defined system that allows authorized users easy access?	Accounting records and supporting documents are retained for 1–2 years for audit purposes and subsequently archived for 10 years. Only authorized staff with pass keys have access to records and documents.	Low
4.7 Describe any previous audit findings that have not been addressed.	The MECSS does not have any audit issues from the last 2 years that have not been addressed.	Low
Segregation of Duties		

Topic	Response	Potential Risk Event
4.8 Are the following functional responsibilities performed by different units or persons: (i) authorization to execute a transaction; (ii) recording of the transaction; (iii) custody of assets involved in the transaction; (iv) reconciliation of bank accounts and subsidiary ledgers?	Yes, all these transactions are performed by different staff members at the MECSS.	Low
4.9 Are the functions of ordering, receiving, accounting for, and paying for goods and services appropriately segregated?	Yes, all these transactions are performed by different staff members at the MECSS. It is not clear that there are strong internal controls over goods received. The PIU will need to develop strong internal controls to ensure goods and services received match the contract requirements.	Substantial
Budgeting System		
4.10 Do budgets include physical and financial targets?	Yes, The MECSS's budgets have targets for outputs as well as financial or numerical values. The project will have performance and financial targets.	Low
4.11 Are budgets prepared for all significant activities in sufficient detail to allow meaningful monitoring of subsequent performance?	Yes, the MECSS's budgets are prepared as per the formats prescribed by the MOF and are detailed enough to all for performance monitoring. The project budget will also be prepared in an adequate level of detail. To allow the steering committee to monitor performance.	Low
4.12 Are actual expenditures compared to the budget with reasonable frequency? Are explanations required for significant variations against the budget?	This data is stored in the GFMS and reports can be produced from the system. Variations in the budget are not permitted.	Low
4.13 Are approvals for variations from the budget required (i) in advance, or (ii) after the fact?	The system does not allow for transactions that would result in expenditures exceeding the budgeted amount for any budget line. Budget adjustments can be requested in advance up to 20% for a particular budget line but must be approved by the MOF before an expenditure can be processed. Funds may not be moved from one project to another and other rules apply.	Low
4.14 Is there a ceiling, up to which variations from the budget may be incurred without obtaining prior approval?	No variations are allowed without prior approvals.	Low

Topic	Response	Potential Risk Event
4.15 Who is responsible for preparation, approval and oversight/monitoring of budgets?	The MECSS's budgets are prepared by the Department of Finance and Economics. MECSS senior management participates in the process and approves the final budget. It is then reviewed by the MOF who prepares the consolidated budget for the government. It is then approved by the State Great Khural. Budget execution is controlled and monitored by the MECSS management and reports are submitted to the MOF as required.	Low
4.16 Describe the budget process. Are procedures in place to plan project activities, collect information from the units in charge of the different components, and prepare the budgets?	The MECSS has several staff in the Department of Finance and Economics who prepared different parts of the budget. They collaborate with various technical staff and department heads to prepare budgets with performance objectives that are linked with funding.	Low
4.17 Are the project plans and budgets of project activities realistic, based on valid assumptions, and developed by knowledgeable individuals?	Yes, technical staff work with financial professionals to prepare the budgets.	High
Is there evidence of significant mid-year revisions, inadequate fund releases against allocations, or inability of the EA to absorb/spend released funds?	No, the MECSS has made unusual requests for budget revisions.	
Is there evidence that government counterpart funding is not made available adequately or on a timely basis in prior projects?	Counterpart contributions are expected to be "in kind".	
What is the extent of over- or under-budgeting of major heads over the last 3 years? Is there a consistent trend either way?	Minimal evidence of inaccurate budgeting in the last year.	
Payments		
4.18 Do invoice-processing procedures require: (i) Copies of purchase orders and receiving reports to be obtained directly from issuing departments? (ii) Comparison of invoice quantities, prices and terms, with those indicated on the purchase order and with records of goods actually received? (iii) Comparison of invoice quantities with those indicated on the receiving reports? (iv) Checking the accuracy of calculations? (v) Checking authenticity of invoices and supporting documents?	The payment documents include the purchase order, the invoice, and the delivery note. All of these are checked and approved by MECSS staff before the payment is authorized. Goods receipt is only checked by one person, a second person familiar with the process and technical knowledge, if necessary should also check goods.	Low

Topic	Response	Potential Risk Event
4.19 Are all invoices stamped PAID, dated, reviewed and approved, recorded/entered into the system correctly, and clearly marked for account code assignment?	Yes, invoices are reviewed and approved by adequate staff and there are adequate internal controls. Purchase orders are created and stored in the GFMS and checked before payments are approved.	Low
4.20 Do controls exist for the preparation of the payroll? Are changes (additions/deductions/modifications) to the payroll properly authorized?	Yes, the payroll and changes are reviewed and approved by the State Secretary and the Chief Accountant.	Low
Policies and Procedures		
4.21 What is the basis of accounting (e.g., cash, accrual) followed (i) by the entity? (ii) By the project?	The MECSS uses accrual accounting.	Low
4.22 What accounting standards are followed (International Financial Reporting Standards, International Public Sector Accounting Standards – cash or accrual, or National Accounting Standards (specify) or other?	IPSAS, International Public Sector Accounting Standards (accrual)	Low
4.23 Does the project have adequate policies and procedures manual(s) to guide activities and ensure staff accountability?	Policies and procedure manuals will be developed by the PIU for the project administration.	Low
4.24 Is the accounting policy and procedure manual updated regularly and for the project activities?	The accounting policy and procedure manual for the MECSS is updated regularly. The manual for the project will be updated regularly.	Low
4.25 Do procedures exist to ensure that only authorized persons can alter or establish a new accounting policy or procedure to be used by the entity?	These changes are controlled by the MOF and governed by three relevant laws.	Low
4.26 Are there written policies and procedures covering all routine financial management and related administrative activities?	Yes, the MECSS has a manual and one will be created for the project.	Low
4.27 Do policies and procedures clearly define conflict of interest and related party transactions (real and apparent) and provide safeguards to protect the organization from them?	Yes, the MECSS has policies and procedures with internal controls and mechanisms to prevent conflicts of interest.	Low
4.28 Are manuals distributed to appropriate personnel?	Yes, manuals are distributed to the appropriate staff.	Low
4.29 Describe how compliance with policies and procedures are verified and monitored.	Compliance with policies and procedures is the responsibility of the MECSS management. The Monitoring, Evaluation and Internal Audit Department at the MECSS is responsible to test procedures and ensure compliance.	Low

Topic	Response	Potential Risk Event
Cash and Bank		
4.30 Indicate names and positions of authorized signatories for bank accounts. Include those persons who have custody over bank passwords, USB keys, or equivalent for online transactions.	The MECSS State Secretary Bayarsaikhan.B, Head of Finance and Economics, Chief Accountant Gantsetseg.Kh, Accountant Altantuya.R are signatories of the bank accounts.	Low
4.31 Does the organization maintain an adequate and up-to-date cashbook recording receipts and payments?	The MECSS maintains a cashbook through the GFMS. The PIU will maintain a cashbook for the project.	Low
4.32 Describe the collection process and cash handling procedures. Do controls exist for the collection, timely deposit and recording of receipts at each collection location?	Not applicable. The MECSS does not keep cash on hand. They only receive funds from the government budget. Receipts are carefully controlled.	Low
4.33 Are bank accounts reconciled on a monthly basis? Or more often?	Bank accounts are reconciled every month and they are up to date.	Low
Is cash on hand physically verified, and reconciled with the cash books? With what frequency is this done?	The MECSS keeps no cash on hand, they keep all their funds in the bank.	
4.34 Are all reconciling items approved and recorded?	Yes.	Low
4.35 Are all unusual items on the bank reconciliation reviewed and approved by a responsible official?	Yes.	Low
4.36 Are there any persistent/non-moving reconciling items?	No.	Low
4.37 Are there appropriate controls in safekeeping of unused cheques, USB keys and passwords, official receipts and invoices?	Yes, they do not use cheques, only bank transfers.	Low
4.38 Are any large cash balances maintained at the head office or field offices? If so, for what purpose?	No.	Low
4.39 For online transactions, how many persons possess USB keys (or equivalent), and passwords? Describe the security rules on password and access controls.	They do not do online transactions.	Low
Safeguard over Assets		
4.40 What policies and procedures are in place to adequately safeguard or protect assets from fraud, waste and abuse?	All assets are recorded on the GFMS system when purchased. Each asset is tagged and when handed to a staff member it is recorded.	High

Topic	Response	Potential Risk Event
4.41 Does the entity maintain a Fixed Assets Register? Is the register updated monthly? Does the register record ownership of assets, any assets under lien or encumbered, or have been pledged?	Yes, but only the GFMIS. It is not clear that this is sufficiently detailed to actually track and control assets. A record of assets handed over to staff is made but it is not clear that this is updated.	High
4.42 Are subsidiary records of fixed assets, inventories and stocks kept up to date and reconciled with control accounts?	They do not appear in any asset register or other systems, to track and control assets, other than the records in the GFMIS. Fixed assets are checked against the record in the GFMIS twice a year which means there is a system to monitor assets.	High
4.43 Are there periodic physical inventories of fixed assets, inventories and stocks? Are fixed assets, inventories and stocks appropriately labeled?	Yes, fixed assets are checked against the GFMIS records twice a year.	High
4.44 Are the physical inventory of fixed assets and stocks reconciled with the respective fixed assets and stock registers, and discrepancies analyzed and resolved?	Yes, fixed assets are checked against the GFMIS records twice a year. The record in the GFMIS is a sort of asset register but it does not record a lot of details about the asset.	High
4.45 Describe the policies and procedures in disposal of assets. Is the disposal of each asset appropriately approved and recorded? Are steps immediately taken to locate lost, or repair broken assets?	A list of assets to be disposed of is approved by the State Secretary. Disposal is controlled by the Head of the Finance and Economics Department and the disposal is recorded in the GFMIS.	High
4.46 Are assets sufficiently covered by insurance policies?	Yes, they have insurance.	High
4.47 Describe the policies and procedures in identifying and maintaining fully depreciated assets from active assets.	All assets are recorded on the GFMIS, fully depreciated or not until disposed of.	High
Other Offices and Implementing Entities		
4.48 Describe any other regional offices or executing entities participating in implementation.	The Ulaanbaatar Municipal Education Department and the Procurement Department of the Municipal Government of Ulaanbaatar will be involved in procurements and on procurement committees.	Low
4.49 Describe the staff, their roles and responsibilities in performing accounting and financial management functions of such offices as they relate to the project.	Only the MECSS and PIU will be involved in the financial management of the project.	Low

Topic	Response	Potential Risk Event
4.50 Has the project established segregation of duties, controls and procedures for flow of funds and financial information, accountability, and reporting and audits in relation to the other offices or entities?	No other offices will handle project funds.	Low
4.51 Does information among the different offices/ implementing agencies flow in an accurate and timely fashion? In particular, do the offices other than the head office use the same accounting and reporting system?	The PIU will coordinate information flows between agencies involved in the project.	Low
4.52 Are periodic reconciliations performed among the different offices/implementing agencies? Describe the project reporting and auditing arrangements between these offices and the main executing/implementing agencies.	Not applicable.	Low
4.53 If any sub-accounts (under the Imprest Account) will be maintained, describe the results of the assessment of the financial management capacity of the administrator of such sub-accounts.	There will be one sub-account set up under the imprest account at a reputable commercial bank.	Low
Contract Management and Accounting		
4.54 Does the agency maintain contract-wise accounting records to indicate gross value of contract, and any amendments, variations and escalations, payments made, and undisbursed balances? Are the records consistent with physical outputs/deliverables of the contract?	There does not appear to be an agreed procedure in place to monitor contract progress and performance. The PIU must have procedures in place to monitor and control contracts with multiple payments and various outputs and stages. The PIU will need a procedure in place to ensure contractors have met the technical requirements of each stage before an invoice/payment is made.	Substantial
4.55 If contract records are maintained, does the agency reconcile them regularly with the contractor?	Yes, all requests for payments from contractors are reviewed and agreed with the contractor before payment is made.	Low
Other		
4.56 Describe project arrangements for reporting fraud, corruption, waste and misuse of project resources. Has the project advised employees, beneficiaries and other recipients to whom to report if they suspect fraud, waste or misuse of project resources or property?	Fraud, corruption, waste, and misuse of project resources will be reported to the government and ADB by the MECSS and PIU.	Low

Topic	Response	Potential Risk Event
5. Internal Audit		
5.1 Is there an internal audit (IA) department in the entity?	The MECSS has a Monitoring, Evaluation and Internal Audit Department with four internal auditors.	Low
5.2 What are the qualifications and experience of the IA staff?	There is a Head of Monitoring, Evaluation and Internal Audit Department, four internal auditors and four staff engaged in monitoring and evaluation. All the auditors have a background in accounting and some have legal experience. All of them have experience working in government agencies.	Substantial
5.3 To whom does the head of the internal audit report?	The Head of the Monitoring, Evaluation and Internal Audit Department reports to the State Secretary. Reports are submitted to the Minister.	Low
5.4 Will the internal audit department include the project in its annual work program?	Yes, they will included it in the audit plan for the year approved by the minister.	Low
5.5 Are actions taken on the internal audit findings?	In general, action has been taken to address previous findings in particular serious issues, such as fraud, have been addressed.	Substantial
5.6 What is the scope of the internal audit program? How was it developed?	They cover all entities under the MECSS all schools, sports facilities and departments in the MECSS. They make an annual plan but also respond to specific requests where there are concerns.	Substantial
5.7 Is the IA department independent?	It is separate from the Finance and Economics Department but they both report to the State Secretary of the MECSS. Reports are submitted directly to the minister.	Low
5.8 Do they perform pre-audit of transactions?	No but this should not be necessary if proper internal controls are in place and the internal controls are tested and improved by the internal auditors.	Low
5.9 Who approves the internal audit program?	The minister.	Low
5.10 What standards guide the internal audit program?	National standards on auditing.	Low
5.11 How are audit deficiencies tracked?	The department is responsible to follow up on audits and monitor responses to audit issues. While there should be an Audit Committee to follow up on audits at the MECSS. One has not been established yet. They plan to establish one.	Substantial

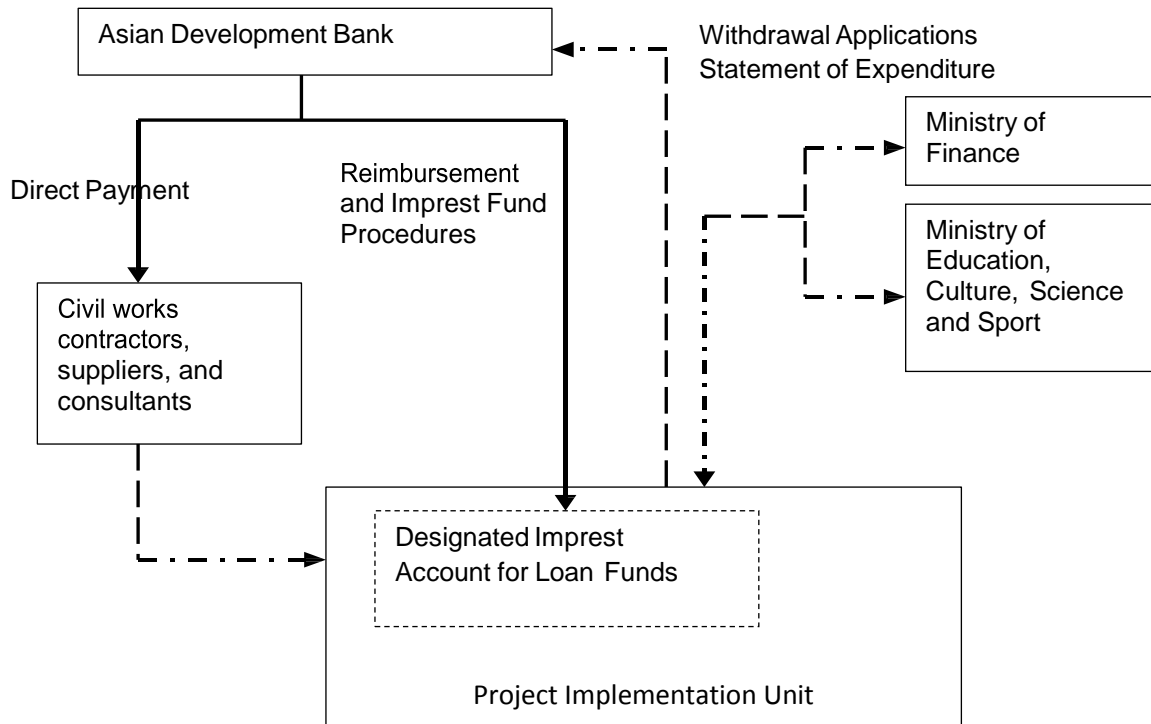
Topic	Response	Potential Risk Event
5.12 How long have the internal audit staff members been with the organization?	The department head has been at MECSS for less than a year but one auditor has been there for 5 years the other three less than one year.	Low
5.13 Does any of the internal audit staff have an IT background?	No.	Substantial
5.14 How frequently does the internal auditor meet with the audit committee without the presence of management?	While there should be an Audit Committee to follow up on audits at the MECSS, one has not been established yet. They plan to establish one.	Substantial
5.15 Has the internal auditor identified / reported any issue with reference to availability and completeness of records?	No.	Substantial
5.16 Does the internal auditor have sufficient knowledge and understanding of ADB's guidelines and procedures, including the disbursement guidelines and procedures (i.e., LDH)?	One auditor has knowledge of ADB guidelines and experience auditing ADB projects.	Substantial
6. External Audit – entity level		
6.1 Is the entity financial statement audited regularly by an independent auditor? Who is the auditor?	Yes, they are audited every year by the National Audit Office.	Low
6.2 Are there any delays in audit of the entity? When are the audit reports issued?	No, they are issued a few months after the financial statements are finalized.	Low
6.3 Is the audit of the entity conducted in accordance with the International Standards on Auditing, or the International Standards for Supreme Audit Institutions, or national auditing standards?	Audits are conducted in accordance with the International Standards on Auditing.	Low
6.4 Were there any major accountability issues noted in the audit report for the past three years?	Yes, there were some significant issues with funds and resources misused but all of the issues were addressed.	Low
6.5 Does the external auditor meet with the audit committee without the presence of management?	While there should be an Audit Committee at the MECSS one has not been established yet. The do plan to establish one.	Low
6.6 Has the entity engaged the external audit firm for any non-audit engagements (e.g., consulting)? If yes, what is the total value of non-audit engagements, relative to the value of audit services?	No.	Low

Topic	Response	Potential Risk Event
6.7 Has the external auditor expressed any issues on the availability of complete records and supporting documents?	No.	Low
6.8 Does the external auditor have sufficient knowledge and understanding of ADB's guidelines and procedures, including the disbursement guidelines and procedures (i.e., LDH)?	Yes. The National Audit Office staff have knowledge and understanding of ADB's guidelines and procedures and significant experience with ADB projects.	Low
6.9 Are there any material issues noted during the review of the audited entity financial statements that were not reported in the external audit report?	No.	Low
External Audit – project level		
6.10 Will the entity auditor audit the project accounts or will another auditor be appointed to audit the project financial statements?	The National Audit Office will likely appoint and an external auditor to audit the project. They will be approved by the ADB.	Low
6.11 Are there any recommendations made by the auditors in prior project audit reports or management letters that have not yet been implemented?	No. Under past ADB-financed projects in the MECSS, actions were taken to correct any issues noted.	Low
6.12 Is the project subject to any kind of audit from an independent governmental entity (e.g. the supreme audit institution) in addition to the external audit?	No.	Low
6.13 Has the project prepared acceptable terms of reference for an annual project audit? Have these been agreed and discussed with the EA and the auditor?	These will need to be prepared by the PIU and agreed by the MECSS and the auditor.	Low
6.14 Has the project auditor identified any issues with the availability and completeness of records and supporting documents?	No.	Low
6.15 Does the external auditor have sufficient knowledge and understanding of ADB's guidelines and procedures, including the disbursement guidelines and procedures (i.e., LDH)?	Yes. The external auditor should have experience in auditing ADB projects and knowledge of ADB's guidelines.	Low
6.16 Are there any recommendations made by the auditors in prior audit reports or management letters that have not yet been implemented? [For second or subsequent projects]	No. Under past ADB-financed projects in the sector, recommendations made by the auditors were followed up.	Low

Topic	Response	Potential Risk Event
6.17 Were past audit reports complete, and did they fully address the obligations under the loan agreements? Were there any material issues noted during the review of the audited project financial statements and related audit report that have remained unaddressed?	Yes, past projects were audited and there were no audit issues.	Low
7. Reporting and Monitoring		
7.1 Are financial statements and reports prepared for the entity?	Yes. The GFMIS generates financial statements and reports.	Low
7.2 Are financial statements and reports prepared for the implementing unit(s)?	The financial management specialist/accountant of the PIU will prepare financial statements and reports.	Low
7.3 What is the frequency of preparation of financial statements and reports? Are the reports prepared in a timely fashion so as to be useful to management for decision making?	The MECSS prepares quarterly and annual financial reports and present them in a timely manner for management decision-making. This will also be adopted for the project.	Low
7.4 Does the entity reporting system need to be adapted for project reporting?	No. The PIU will use similar procedures but they will use a separate accounting software to store data and prepare reports.	Low
7.5 Has the project established financial management reporting responsibilities that specify the types of reports to be prepared, the report content, and purpose of the reports?	The financial management specialist/accountant of the PIU will prepare financial reports as required by the ADB and the Project Administration Manual.	Low
7.6 Are financial management reports used by management?	Yes.	Low
7.7 Do the financial reports compare actual expenditures with budgeted and programmed allocations?	Yes, budget and expenditure data is stored and comparative reports are created from the GFMIS.	Low
7.8 How are financial reports prepared? Are financial reports prepared directly by the automated accounting system or are they prepared by spreadsheets or some other means?	The MECSS's final financial reports are prepared using spreadsheets with the data from the GFMIS. For the project the PIU will generate financial reports using accounting software.	Low
7.9 Does the financial system have the capacity to link the financial information with the project's physical progress? If separate systems are used to gather and compile physical data, what controls are in place to reduce the risk that the physical data may not synchronize with the financial data?	The GFMIS stores financial data only. For the project, a separate project performance monitoring and reporting system will be established in sync with project budget and expenditure data.	Low

Topic	Response	Potential Risk Event
7.10 Does the entity have experience in implementing projects of any other donors, co-financiers, or development partners?	Yes, they have completed a number of ADB projects and some are in progress. Project details are above.	Low
8. Information Systems		
8.1 Is the financial accounting and reporting system computerized?	Yes, MECSS uses the government's GFMS software. The PIU will manage the project outside of the GFMS system.	Low
8.2 If computerized, is the software off-the-shelf, or customized?	Customized. The PIU will install an off-the shelf software as donor funds are managed outside the government system.	Low
8.3 Is the computerized software standalone, or integrated and used by all departments in the headquarters and field units using modules?	The GFMS is integrated and used by all ministries. For the project, software will be installed at the PIU to be located in Ulaanbaatar.	Low
8.4 How are the project financial data integrated with the entity financial data? Is it done through a module in the enterprise financial system with automatic data transfer, or does it entail manual entry?	The project financial data will not be integrated with the MECSS's financial data. Donor funds are managed outside the government system.	Low
8.5 Is the computerized software used for directly generating periodic financial statements, or does it require manual intervention and use of Excel or similar spreadsheet software?	Final reports are prepared outside the system with data from the system. For the project accounting software, should be used that will not be connected directly to the GFMS.	Low
8.6 Can the system automatically produce the necessary project financial reports?	The PIU should use accounting software to generate reports automatically and store data securely.	Low
8.7 Is the staff adequately trained to maintain the computerized system?	MECSS staff are adequately trained in the use of GFMS. The financial management specialist/accountant for the PIU should have experience in maintaining and using the accounting software.	Substantial
8.8 Do the management, organization and processes and systems safeguard the confidentiality, integrity and availability of the data?	Yes, the GFMS is password protected and procedures are in place to protect data. The PIU will have appropriate procedures.	Low
8.9 Are there back-up procedures in place?	The GFMS is maintained and backed up by the MOF. The PIU will have to have backup procedures for project data.	Low
8.10 Describe the backup procedures – online storage, offsite storage, offshore storage, fire, earthquake, and calamity protection for backups.	Documents are kept in disaster resistant room/cabinets. The Mongolian National Data Center keeps the MECSS electronic data secure for long term storage.	Low

APPENDIX 2: FUND FLOW DIAGRAM



————▶ Funds Flow

- · - · - · ▶ Document Flow