

FINANCIAL MANAGEMENT ASSESSMENT

Executive Summary

A financial management assessment (FMA) has been prepared in accordance with Asian Development Bank's (ADB) Guidelines for *the Financial Management and Analysis of Projects* (2005) and *the Financial Due Diligence; A Methodology Note* (2009); and *the Financial Management Technical Guidance Note* (2015) for the proposed Secondary Towns Urban Development Project (STUDP).

The FMA considered the financial management capacity of the Ministry of Works and Human Settlements (MOWHS) in its role as the executing agency, focusing on fund flows, staffing, accounting policies and procedures, internal controls, financial reporting and monitoring, and internal and external audits. The MOWHS has considerable experience in implementing multilateral donors assisted projects including the completed Urban Infrastructure Development Project and the ongoing the Urban Infrastructure Project funded by ADB.

The project management unit (PMU) based in the Department of Engineering Services (DES) of the MOWHS has already been created with a project director, a project coordinator and a fulltime project manager. The PMU will be responsible for all day-to-day management of STUDP, including but not limited to: (i) preparing an overall project implementation plan and detail work program; (ii) providing overall monitoring and guidance on the implementation; (iii) monitoring and supervising all management activities; (iv) preparing project progress and project completion reports; (v) financial planning and budgeting including contract awards and disbursements; and (vi) ensuring full compliance with ADB's resettlement, environmental and other safeguard policies.

The project implementing units (PIUs) located within the three project municipalities will be responsible, under the guidance and supervision of the PMU, for: (i) project management and administration, (ii) the day-to-day contract management functions of the project which shall include compliance to the requirements of the contract documents, (iii) supervision and monitoring of construction and consulting works, (iv) ensuring safeguards compliance, and (v) quality control as required by the contract documents. The PIUs will be headed by a project manager who will be supported by a construction supervision coordinator.

The major risk factors identified during the assessment that need to be addressed include:

- (i) lack of training to new accounting staff of PMU may cause delays in preparing day-to-day financial management; and
- (ii) limitations of the existing accounting system may delay submission of periodic financial reports.

Despite the highlighted risks, the financial management arrangements of MOWHS and its PMU are satisfactory, taking the ongoing actions of MOWHS in consideration. In addition, the project consultants will support MOWHS and its PMU in enhancing their financial management capacity. The overall risk assessment for the STUDP is "moderate". The action plans to reduce the above risks include:

- (i) extending full training and capacity building support for enhancing the financial management capacity of PMU; and
- (ii) procuring a suitable accounting package for establishing better reporting and monitoring system.

I. INTRODUCTION

1. A financial management assessment (FMA) was prepared in accordance with Asian Development Bank's (ADB) *Guidelines for the Financial Management and Analysis of Projects (2005)*,¹ and the *Financial Due Diligence: A Methodology Note (2009)*,² and the *Financial Management Technical Guidance Note (2015)*,³ focusing on fund flows, staffing, accounting policies and procedures, internal controls, financial reporting and monitoring, and internal and external audits.
2. The FMA considered the financial management capacity of the Ministry of Works and Human Settlements (MOWHS) in its role as the executing and implementing agency. The MOWHS has considerable experience in implementing donors assisted projects including the completed Urban Infrastructure Development Project (UIDP) and the ongoing the Urban Infrastructure Project (UIP) funded by ADB. All project disbursements and the related project accounting and reporting will be done by MOWHS and its project management unit (PMU).
3. The MOWHS, along with its PMU, will be responsible for all day-to-day management of the proposed Secondary Towns Urban Development Project (STUDP), which include: (i) preparing an overall project implementation plan and detail work program; (ii) providing overall monitoring and guidance on the implementation; (iii) monitoring and supervising all management activities; (iv) preparing project progress and project completion reports; (iv) financial planning and budgeting including contract awards and disbursements; and (v) ensuring full compliance with ADB's resettlement, environmental and other safeguard policies.
4. The project implementing units (PIU) located within the three municipalities will be responsible, under the guidance and supervision of the PMU, for: (i) project management and administration, (ii) the day to day contract management functions of the project which shall include compliance to the requirements of the contract documents, (iii) supervision and monitoring of construction and consulting works, (iv) ensuring safeguards compliance, and (v) quality control as required by the contract documents. The PIUs will be headed by a Project Manager who will be supported by a construction supervision coordinator.
5. A key aspect of the FMA is evaluating the risks associated with project financial management arrangements. ADB's principal concern is to ensure that project funds are used economically and efficiently for the purposes intended. In support of this, it seeks assurance that the financial management system of the MOWHS and its PMU can report on the source and use of the project funds. The assessment was based on the results of the FMA questionnaire and discussions with officials of the MOWHS and its PMU. Information were collected through various reports, including audit reports of previous ADB projects implemented through the MOWHS.
6. This FMA was conducted to: (i) assess the capacity of the MOWHS and its PMU to monitor, manage, and support the overall project; (ii) assess the capacity of the MOWHS and its PMU to implement the project; and (iii) propose ways and means to strengthen the capacity of the MOWHS and its PMU. Specifically, the objective is to enhance competence levels to achieve the government's goals of improved access to urban services with required climate resiliency of the project municipalities.

¹ ADB. 2005. *Financial Management and Analysis of Projects*. Manila.

² ADB. 2009. *Financial Due Diligence: A Methodology Note*. Manila.

³ ADB. 2015. *Financial Management Technical Guidance Note*. Manila.

II. BRIEF PROJECT DESCRIPTION

7. The impact of STUDP will be balanced and sustainable development of human settlements in Samdrup Jongkhar, Sarpang, and Trashigang ensured. The outcome will be quality, efficiency, and sustainability of urban services improved. The STUDP will have the following two outputs: (i) urban infrastructure expanded and/or upgraded; and (ii) capacity of institutions and local communities strengthened.

8. The STUDP will provide the improved water supply services in Samdrup Jongkhar, Sarpang, and Trashigang, and sewerage systems in Samdrup Jongkhar and Trashigang. Infrastructure for new and improved urban housing and commercial developments will be supported in Sarpang. Community-based solid waste management programs focusing on segregation at source will be provided in Sarpang and Trashigang and solid waste and sanitation equipment provided to all three municipalities. Capacity building will also be provided to implementation and operation and maintenance personnel in each municipality to enhance sustainability of the assets established under STUDP.

III. COUNTRY FINANCIAL MANAGEMENT ISSUES

9. The 2008 Constitution lays down the principles for Public Financial Management (PFM) including the establishment of (i) the Royal Audit Authority (RAA) “to audit and report on the economy, efficiency, and effectiveness in the use of public resources”; and (ii) the Public Accounts Committee “to review and report on the Annual Audit Report to Parliament”.

10. The key legislation on PFM is the Public Finance Amendment Act of 2014 which regulates financial management for the effective and efficient use of public resources, accountability and fiscal policy and vests the overall responsibility for managing the public finances with the Council of Ministers. The Financial Rules and Regulations (FRR) 2001 is a set of over-arching documents governing PFM in Bhutan and consists of a main document, the Financial Management Manual and six technical documents, the Finance and Accounting Manual, the Budget Manual, the Aid and Debt Management Manual, the Property Management Manual, the Procurement Manual, and the Revenue Manual. A more recent version of the Financial Management Manual was released in 2016.

11. The Public Finance Act, read with the FRR, empowers the Ministry of Finance (MOF) to set the government accounting standards and determine the financial reporting framework. Revenue and expenditure accounting and control are done on computerized applications that also determine the control activities. MOF is the parent agency for a government-wide internal audit function. An Internal Audit Central Coordinating Agency administratively reports to the Finance Secretary and to the high-level Committee of Secretaries.

12. The municipal finance policy (2012) discusses how municipalities can achieve sustainability through its key provisions which state that ⁴ (i) all charges shall be set to cover the costs of the service including salaries, use of utilities, transportation, materials, maintenance and depreciation (re-investment); and (ii) the present subsidy for current expenditures will be eliminated gradually (up to the Eleventh Five-Year Plan which ends in 2018). At that time, current expenditures will be financed fully from municipalities’ own revenues.

⁴ Municipal (Thromde Class A) Finance Policy, Bhutan.

13. The annual financial statements (AFS) of the government are prepared by the Department of Public Accounts, MOF. Audit of the Government in Bhutan is governed by the Audit Act, 2006. The AFS are audited by the RAA, which submits an annual audit report on the AFS to the Parliament.

14. The World Bank's Country Partnership Strategy (CPS)⁵ notes that Bhutan continues to strengthen its governance framework as it moved further up on Transparency International's Corruption Perceptions Index, from 38 to 33. In recognition of additional steps, it has taken to strengthen its anti-corruption legal framework, including passage of the 2011 Anti-Corruption Act, the establishment of an Anti-Corruption Commission (ACC) and further strengthening rules governing asset declaration by public servants in 2012.

15. However, the World Bank's CPS also identifies risks related to capacity constraints given Bhutan's small human resource base and limited number of trained people with high-level managerial capacity. In light of this, the Bank is working with the Government to build the use of country systems through a limited number of Bank and International Finance Corporation (IFC) financed operations, coupled with continual technical support and training, particularly for fiduciary functions (i.e., financial management and procurement).

16. ADB's Bhutan CPS⁶ provides ADB's strategic approach in Bhutan for 2014-2018, aligned with the midterm review of Strategy 2020, the country's own development strategy, and ADB's comparative strengths. The CPS was based on the CPS final review⁷ in which ADB country operations and programs in Bhutan were rated *successful* by both a country assistance performance evaluation conducted in 2010 and the CPS final review validation report in 2013. However, while the 2010 ADB Country Assistance Program Evaluation⁸ (CAPE) gave ADB country operations and programs in Bhutan an overall rating of *successful*, the programs were also rated as *less likely sustainable* due in part to the fact that charging cost-reflective tariffs, user fees, or interest rates has not been considered desirable or necessary in Bhutan.

17. The CPS reports on risk assessment for Bhutan are as follows (footnote 6):

- (i) **Governance risks.** Bhutan is in the middle of a rapid transformation and has planned an ambitious public investment program for the CPS period (2014–2018) that will put the national governance infrastructure under considerable pressure. However, despite vulnerabilities in some parts of the systems in the three sectors (energy, finance, and transport) and for the major themes (public financial management, public procurement, and anticorruption) covered by the risk assessment for this CPS, no serious governance risks exist that could jeopardize the development impact of ADB operations in the country; and
- (ii) **Public financial management, public procurement, and anticorruption.** Bhutan's public financial management system is more robust than those of many comparable countries, but capacity in financial management is weak at the local level. Procurement vulnerabilities reside in the inability of the institutions and staff involved to fully apply enhanced rules and regulations, and a lack of government capacity to effectively implement increasingly complex procurement packages in some key sectors. Some vulnerability to corruption remains because of weakness in internal accountability measures.

⁵ World Bank. 2013. [Country Partnership Strategy Progress Report for the Kingdom of Bhutan for the period FY11-14](#).

⁶ ADB. 2014. *Country Partnership Strategy: Bhutan, 2014-2018*. Manila.

⁷ ADB. 2013. *Country Partnership Strategy Final Review: Bhutan, 2010-2012*. Manila.

⁸ ADB. 2010. *Country Assistance Program Evaluation for Bhutan (2010)*. Manila.

18. Risk mitigation measures, specified for the interim CPS 2012–2013, continue to remain valid. These mainly involve capacity enhancement, particularly at the local level, and the strengthening of internal controls in public sector agencies.

19. **Reform Strategy.**⁹ Bhutan prepared a PFM Reform Program/Strategy in 2012 covering a comprehensive, sequenced and time-bound action plan to bring about improvements in the PFM systems and processes in line with international standards. Development partners have actively supported Bhutan's initiatives to strengthen PFM. The World Bank and other development partners, including IMF, EU, ADA, SECO, UNDP, and ADB have been actively partnering, largely on a bilateral approach, to strengthen PFM in Bhutan. The interventions include: (i) support in the development of an e-payment gateway; (ii) strengthening budget preparation process; (iii) treasury management and cash flow forecasting; (iv) macro-fiscal management (by the IMF); (v) supporting the development of internal audit; (vi) inter-governmental fiscal transfers; (vii) implementation of Bhutan Accounting Standards and development of a PFM reform group (by the World Bank); (viii) supporting development of a Revenue Administration and Information Management System and an Audit Resource Management System for the supreme audit institution; (ix) technical support on debt sustainability analysis and macro-fiscal regulation (by the ADB); and (x) supporting judiciary, CSO and Supreme Audit Institution (ADA) and local government strengthening with support from the European Union. Recently, the seeds for the establishment of a PFM Multi-Donor Fund (MDF) has been sown, led by the World Bank, with the objective of aligning support of development partners in Bhutan for joint dialogue and efforts in implementing a government-owned PFM reform strategy.

IV. PROJECT FINANCIAL MANAGEMENT SYSTEM

20. **Major experiences in managing externally financed projects.** The MOWHS has implemented various projects funded by the World Bank, ADB, DANIDA, HELVETAS, WFP, UNDP, WHO, Government of India, and Government of Netherlands. MOWHS completed the UIDP funded by ADB in December 2014 and has been implementing the ongoing UIP funded by ADB since 2013.

21. **Funds Flow Arrangements.** The proposed loan will follow the current funds flow arrangements for ADB funded UIP whereby ADB Loan funds are transferred from ADB to the advance account with the Royal Monetary Authority (RMA) of Bhutan. The RMA transfers funds to the DPA and the DPA transfers these funds to the Project Account in the Bank of Bhutan. This Project Account is maintained as Project Letter of Credit Account in the name of the MOWHS. The government funds are also deposited in this project account which contains funds from both sources.

22. **Staffing.** The MOWHS will manage the project through its Project Management Unit (PMU) which will be reporting directly to the Water Supply Division (WSD) under the Department of Engineering Services (DES). The PMU has already been established with a Project Director, a Project Coordinator and a fulltime Project Manager. They will be supported by individual and firm consultants.

23. The project accounts will be maintained by the Accounts Division, which is under the Directorate of Service of MOWHS. It is headed by a Deputy Chief Accounts Officer, assisted by an Accounts Officer and supported by seven Accountants. Under the ongoing ADB funded UIP,

⁹ World Bank. 2016. *Bhutan Public Financial Management Assessment Report*. Washington, D.C.

project accounts are being handled by an Accounts Assistant acting as the Project Accountant for ADB Projects. The division is adequately staffed but will need additional staff once new projects will be undertaken.

24. Based on the MOF's policy, accounting staff are rotated every 3 years. The MOF usually assigns staff to the agency to handle project accounting. In previous ADB projects, the PMU experienced difficulties in handling project disbursements and reporting whenever new staff were assigned to the project. For STUDP, MOWHS will request MOF to assign one Project Accountant to the PMU upon the implementation.

25. **Segregation of duties.** The MOWHS's organizational system ensures adequate segregation of duties. Under the ongoing ADB funded UIP, the project transactions are segregated as follows:

- (i) transactions evidenced by Contractors' Bills are verified by the PIUs/PMU;
- (ii) the voucher for payment is approved by the Disbursement Officer;
- (iii) recording and reconciliation of bank accounts and subsidiary ledgers are performed by the concerned accountants and supervised by the Accounts Officer; and
- (iv) custody of assets is the responsibility of the PIU/PMU and concerned store in-charged.

26. **Accounting policy and procedures.** The MOWHS accounts are maintained on a cash basis following the Government Financial Manual 2001. Financial Reports are generated by a computerized online accounting system called PEMS (Public Expenditure Management System). Project accounts are part of this program but the program provides very limited data which are not adequate to serve the ADB requirements for disbursement and reporting. The following are the limitations of PEMS:

- (i) PEMS shows annual data but does not have the capacity to show the cumulative expenditure data for multi-year projects;
- (ii) it does not record/report on the physical progress as needed by ADB;
- (iii) it does not record/report on cumulative contract payments and balances;
- (iv) it does not show the amounts in different currencies; and
- (v) it has its own pre-programmed formats for presenting financial statements. As such, the data cannot be linked to an excel program and modified to prepare special project reports.

27. As the results of the above limitations, the PMU consultants in a previous ADB funded UIDP retyped all the project account figures in excel to present the financial statement and other financial information in the ADB prescribed format. This manual procedure caused delays in processing requests for withdrawals and many reconciling errors such that although the project was completed in December 2014, loan closing was significantly delayed.

28. **Budgeting System.** An annual budget call is made during the last quarter of every year by the Department of National Budget (DNB), MOF. Various agencies in the ministry initiate the budget process with reference to the Five-Year Plan and the latest development initiatives. The government including DNB together with the MOWHS conducts mid-term performance review during the third quarter, and the budget for the ensuing fiscal year is finalized for all the agencies and units in the MOWHS, including for externally funded projects. The total budget of MOWHS together with the budget of rest of the government agencies is submitted to the Parliament for approval in every June. A notification of budget approval is circulated by the DNB. Any savings from the current year budget is withdrawn and reverted to the MOF. Fresh budget requisitions are

made to the DPA which releases the funds as per schedule and budget for the subsequent fiscal year.

29. **Payments.** Payments are made against invoices submitted for payments with adequate accounting safeguard procedures and after approval from the internal audit unit.

30. **Cash in Bank.** The Chief Administrative Officer and the Deputy Chief Accounts Officer are the authorized signatories and are responsible for the bank accounts. ADB loan funds will be kept as an advance account of Royal Monetary Authority (RMA) of Bhutan. The RMA will transfer funds to the DPA which will transfer these funds to designated banks of the PMU for STUDP. The government's counterpart funds will also be deposited in this same account. All funds (ADB loan and counterpart funds) released from the government are in the form of Project Letters of Credit (PLC) issued to the designated banks based on the budget and requisitions from the PMU and approved by the Project Director.

31. **Safeguard over assets.** Based on the FRR 2001, the Property Management Manual of the government provides the procedures for the management of Fixed Assets and other inventories including approval and recording of assets disposal. A fixed assets register is maintained and it's updated regularly. There exists periodic verification procedures and insurance provisions for assets.

32. **Other offices and implementing entities.** The implementation of STUDP will be done through PIUs which will be set up in the three towns. The PIUs will be reporting to the PMU.

33. **Contract management and accounting.** Accounts are computerized and maintained on cash basis using PEMS. This includes contract wise accounting records which are however maintained only for a single year. One of the limitations of the PEMs is that it cannot maintain detailed financial records of expenditures for multiyear contracts.

34. **Internal Audit.** Internal audit is conducted by the Internal Audit Unit of MOWHS which is reporting to the Secretary. It is headed by a Chief Internal Auditor and an assistant Internal Auditor. The unit is affiliated with the Central Coordinator of Internal Auditors in the MOF. The unit has a clear job assignment and generally monitors the accounting and the management system of the ministry including pre and post audit of most financial transactions. The latest audit report by the Internal Audit Services Section of MOWHS covers up to the FY 2015. Audit observations and recommendations were made in six areas, including maintenance of documents, consistency in opening bid documents, and lack of due diligence during technical evaluation in one instance.¹⁰ Likewise, the STUDP will also be audited by the Internal Audit Unit of MOWHS.

35. **External Audit–Entity Level.** The MOWHS accounts are audited by the RAA on an annual basis. The RAA has its own auditing standard based on the Audit Act of 2006. They adopt Generally Accepted Auditing Practices and other related rules that are consistent with the international auditing standards. The audit report for FY 2016 was issued by RAA in March 2017. The Audit Report revealed no major findings.

36. **External Audit–Project Level.** The RAA normally audits the accounts of externally funded projects within 6 months after the end of each fiscal year. The latest audited project

¹⁰ ADB. 2016. *Report and Recommendation of the President to the Board of Directors: Proposed Grant to the Kingdom of Bhutan for the Thimphu Road Improvement Project*. Financial Management Assessment (accessible from the list of linked documents in Appendix 2). Manila.

financial statement (APFS) of ADB-funded projects was for the UIP covering the period of FY 2016-17. The audit was conducted August 2017 and the report was issued October 2017. This was submitted timely to ADB without any delays. The project accounts of STUDP will also be audited by RAA.

37. **Reporting and Monitoring.** Reporting is done in accordance with accounting standards, i.e., the GAAP and the Bhutan Accounting Standards, which are the bases for the Government Financial Manual 2001. Financial statements are prepared on a monthly and annual basis using PEMS.

38. **Information Systems.** Accounts are computerized and maintained on cash basis using PEMS. However, the PEMS has several limitations as discussed in para. 26 on accounting policies and procedures.

V. RISK ASSESSMENT

39. The FMA has considered two types of risks: (i) inherent risks; i.e., risks outside the direct control of MOWHS' financial management, and (ii) control risks; i.e., risks concerning the internal functioning and control of MOWHS' Finance and Accounting division. The following key risks have been identified:

Table 1: Risk Assessment

Risk	Risk Assessment	Risk-Mitigation Measures
Inherent Risks		
1. Country-Specific Risks (Bhutan)	<p style="text-align: center;">LOW</p> <ul style="list-style-type: none"> The financial management capacity and auditing standard in Bhutan are sound. However, the assessment of World Bank in 2016 revealed the necessities to further improve in the areas of expenditure composition out-turn, controls over payroll, public access to information, internal audit, legislative scrutiny of annual budget laws and quality and timeliness of annual financial statements.^a 	<ul style="list-style-type: none"> Not applicable
2. Entity-Specific Risks (MOWHS)	<p style="text-align: center;">LOW</p> <ul style="list-style-type: none"> There are strong institutional mechanism and legislative framework for budgeting, accounting, and audit in a time-bound manner. 	<ul style="list-style-type: none"> Not applicable
3. Project-Specific Risks (STUDP)	<p style="text-align: center;">SUBSTANTIAL</p> <ul style="list-style-type: none"> The municipal finance policy (2009) states that all charges shall be set to cover the costs of the service. However, there is the absence of an institutional mechanism whereby tariffs and financial performance are regularly reviewed and monitored. Non-implementation of regular tariff revisions may hamper the sustainability of assets established under STUDP. 	<ul style="list-style-type: none"> The commitment of government to provide sufficient financial support to the project municipalities for covering O&M costs. Preparation and implementation of the systematic plans by project municipalities to enhance revenues and reduce costs.

Risk	Risk Assessment	Risk-Mitigation Measures
Overall Inherent Risk	MODERATE While project-specific risks exist, these risks might be mitigated through efforts of the government and project municipalities with the support of ADB. There is a considerable specific risk in implementing cost recoverable tariffs. The government needs to provide its support to the project municipalities in ensuring the project sustainability.	
Control Risks – MOWHS and PMU		
1. Executing Entity	<p style="text-align: center;">LOW</p> <ul style="list-style-type: none"> • MOWHS has considerable experience in implementing donors assisted projects including the completed UIDP and the ongoing the UIP funded by ADB. • The PMU has already been created with a Project Director, a Project Coordinator, and a fulltime Project Manager. 	<ul style="list-style-type: none"> • Not applicable
2. Flow of Funds	<p style="text-align: center;">LOW</p> <ul style="list-style-type: none"> • Funds flow for STUDP will be similar with the ongoing UIP. There have been no major problems in funds flow of UIP. 	<ul style="list-style-type: none"> • Not applicable
3. Staffing	<p style="text-align: center;">SUBSTANTIAL</p> <ul style="list-style-type: none"> • Inadequate staff capacity in the accounts section and lack of training to new accounting staff may cause delays in day-to-day financial management and submission of periodical financial reports. • A major factor behind this is that trained staff are transferred to other government agencies based on the government's policy of staff rotation every 3 years. 	<ul style="list-style-type: none"> • Extending full training and capacity building support for enhancing the financial management capacity of MOWHS and its PMU.
4. Accounting Policies and Procedures	<p style="text-align: center;">MODERATE</p> <ul style="list-style-type: none"> • The existing accounting system is generally capable of providing the financial information needed by the agency and auditors. • However, it has limitations in providing project accounting data as basis for project disbursements following ADB procedures as follows: <ul style="list-style-type: none"> - it does not show the cumulative expenditure data for multiyear projects, - it can't record/report on the physical progress needed by ADB - it can't record/report on cumulative contract payments and balances. 	<ul style="list-style-type: none"> • Procuring a suitable accounting package for establishing better reporting and monitoring system.
5. Internal audit	<p style="text-align: center;">SUBSTANTIAL</p> <ul style="list-style-type: none"> • MOWHS has three internal auditors reporting to the Minister. They monitor the accounting and the management system of MOWHS. • The latest internal audit report covers the fiscal year of 2015. 	<ul style="list-style-type: none"> • Not applicable

Risk	Risk Assessment	Risk-Mitigation Measures
6. External Audit - project level	<p style="text-align: center;">LOW</p> <ul style="list-style-type: none"> • Annual audit of project accounts is carried out by the RAA. • The latest audited project financial statement of ADB-funded projects was for the UIP covering the FY2017. The audit was conducted August 2017 and the report was issued October 2017. This was submitted timely to ADB without any delay. 	<ul style="list-style-type: none"> • Not applicable
7. External Audit - entity level	<p style="text-align: center;">LOW</p> <ul style="list-style-type: none"> • RAA conducts an annual audit of MOWHS. The latest audit report was issued in March 2017 and covered the FY2015-16. 	<ul style="list-style-type: none"> • Not applicable
7. Reporting and Monitoring	<p style="text-align: center;">MODERATE</p> <ul style="list-style-type: none"> • The existing system has substantial limitations in providing project reports for monitoring since it can't record and report on the physical progress needed by ADB. 	<ul style="list-style-type: none"> • Procuring a suitable accounting package for establishing better reporting and monitoring system.
8. Information Systems	<p style="text-align: center;">MODERATE</p> <ul style="list-style-type: none"> • The existing system has substantial limitations since it does not show the cumulative data for multi-year projects. 	<ul style="list-style-type: none"> • Procuring a suitable accounting package for establishing better reporting and monitoring system.
Overall Control Risk	<p style="text-align: center;">MODERATE</p> <p>Some financial management risks are recognized, but all of them are not high. Providing training to accounts staff, and procuring a suitable accounting package need to be ensured by the government.</p>	

^a Source: World Bank. 2016. *Bhutan Public Financial Management Performance Report: Based on Public Expenditure and Financial Accountability 2016 Framework*. Washington, D.C.

ADB = Asian Development Bank, FY = fiscal year, MOWHS = Ministry of Works and Human Settlements, O&M = operation and maintenance, PMU = project management unit, RAA = Royal Audit Authority, STUDP = Secondary Towns Urban Development Project, UIDP = Urban Infrastructure Development Project, UIP = Urban Infrastructure Project.

VI. STRENGTHS AND WEAKNESS

40. **Strengths.** A significant strength of the financial management system of MOWHS is that it has sufficient experience in handling multilateral funded projects including the on-going ADB funded UIP.

41. **Weaknesses.** The significant weaknesses of the financial management system have been identified and need to be addressed:

- (i) lack of training to new accounting staff of PMU may cause delays in preparing day-to-day financial management; and
- (ii) limitations of the existing accounting system may delay submission of periodic financial reports.

VII. ACTION PLANS

42. The MOWHS and ADB have agreed to an action plan to address the following issues that this FMA identified as shown in Table 2.

Table 2: Action Plan

Area	Current scenario	Risk	Mitigation measure suggested	Target date
Training on ADB requirement	Lack of training to new accounting staff of PMU.	This may cause delays in preparing day-to-day financial management.	Extending full training and capacity building support for enhancing the financial management capacity of MOWHS and its PMU.	July 2018
Project Accounting System	Limitations of the existing accounting system.	This may cause delays in submission of periodic financial reports.	Procuring a suitable accounting package for establishing better accounting and reporting systems.	July 2018

ADB = Asian Development Bank, MOWHS = Ministry of Works and Human Settlements, PMU = project management unit, STUDP = Secondary Towns Urban Development Project.