OFFICE OF INSPECTOR GENERAL

U.S. International Development Finance Corporation

DFC Can Improve Oversight of Renewable Energy and Financing Projects in India

November 13, 2023
Audit Report DFC-24-002-C

1100 New York Avenue, NW
Washington, DC 20527
https://www.dfc.gov/oig

Report Highlights

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

DFC Can Improve Oversight of Renewable Energy and Financing Projects in India

What Was Reviewed

DFC has Invested $3.6 Billion in India

The U.S. International Development Finance Corporation (DFC), Office of Inspector General (OIG) contracted with the independent public accounting firm RMA Associates, LLC (RMA) to conduct a congressionally requested[1] audit of DFC's renewable energy and financing projects. The U.S. House of Representatives Committee on Appropriations requested DFC OIG to complete a follow-up audit similar to U.S. Agency for International Development (USAID) OIG's audit of Overseas Private Investment Corporation's (OPIC) Chile Energy Sector Portfolio completed in 2019.[2] With congressional approval, this audit focused on DFC's renewable energy and financing projects in India, which is the Corporation's largest country investment partner at approximately $3.6 billion. DFC's Office of Accountability is an independent office within DFC that addresses concerns, complaints, or conflicts about environmental or social issues that may arise around DFC-supported projects. The Office of Accountability was consulted during the course of this audit since they issued an internal report in 2018 assessing whether the use of client-reported data, supplemented by selected site visit monitoring, was adequate in achieving program goals.[3]

The objectives were the same as the USAID OIG's audit, which included: (1) determining if DFC involved the U.S. private sector and supported local country development in alignment with its mission; (2) assessing the inputs, data, and analyses used to assess and approve the projects; and (3) assessing the process and internal controls DFC used to identify and mitigate certain risks. 17 projects were evaluated under this audit–eight renewable energy projects and nine financial intermediary projects consisting of financing micro, small, and medium enterprise (MSME) businesses. RMA, together with OIG officials, conducted site visits of four renewable energy and four financial intermediary projects located across India.

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[1] House of Representatives Report 116-444, State, Foreign Operations, And Related Programs Appropriations Bill, 2021 (HR Report 116-444), mandated that DFC OIG submit a report to the Committees on Appropriations assessing the integration and efficiency of policies, procedures, and processes of DFC.
[2] Office of Inspector General, U.S. Agency for International Development, "OPIC Investments Increased Chile's Energy Capacity, but Weak Processes and Internal Controls Diminish OPIC's Ability to Gauge Project Effects and Risks," February 1, 2019; Audit Report No. (9-OPC-19-002-P).
[3] OPIC's Office of Accountability, *Assessment of OPIC's Environmental and Social (E&S) Monitoring of Projects*, February 7, 2018, p. 63.

What Was Found

The audit revealed DFC supported local country development in alignment with its mission and Better Utilization of Investments Leading to Development (BUILD) Act of 2018 requirements. However, DFC did not adequately support a waiver of environmental and social standards for one of the projects reviewed, resulting in $54.91 million in unsupported questioned costs. DFC also has not developed sufficient internal controls to support the approval process for projects financed through subordinated debt. In addition, DFC's records management system can be unreliable when compiling a complete set of documents for individual projects. Finally, DFC has not developed a risk-based assessment to determine which sites to visit or a method to track, report and monitor significant environmental and social events, particularly fatalities and serious injuries. Three fatalities and two serious injuries occurred on one of the reviewed projects.

Recommendations

The audit makes 13 recommendations to DFC's Chief Executive Officer that will further strengthen the integration and efficiency of policies, procedures, and processes regarding renewable energy and MSME financing investments in India. Specifically, RMA recommended that DFC:

- **Recommendation 1:** Revise Directive OD-004 to include the Office of the Chief Risk Officer review of waivers of the DFC Environmental and Social Policy and ensure coordination with the Office of Accountability.
- **Recommendation 2:** Include any waivers of DFC Environmental and Social Covenants as part of the Congressional Notification process.
- **Recommendation 3:** Ensure DFC develops a policy regarding the use of subordinated debt, to include the appropriate uses and approval of subordinated debt.
- **Recommendation 4:** Explicitly incorporate DFC's subordinated debt usage into the Corporation's Enterprise Risk Management process.
- **Recommendation 5:** Until Content Manager and Insight systems interface properly; develop and implement improved internal controls that verify applicable project documents are uploaded in Insight and that appropriate workflows are followed.
- **Recommendation 6:** Ensure the interface between Insight and Content Manager systems is functional so that applicable project documents are readily available and properly stored.
- **Recommendation 7:** Direct DFC's Chief Development Officer and Chief Risk Officer, in coordination with the Office of Accountability, to advise the Office of Development Policy and the Office of Financial and Portfolio Management on strategic goals for annual site visit monitoring. This should include a process for publicly reporting plans, goals, and actual performance.
- **Recommendation 8:** Ensure all divisions update and finalize site visit monitoring policies and procedures to align with the agency's strategic goals.
- **Recommendation 9:** Develop a system to centrally track site visit reporting results that is accessible to staff for cross-monitoring purposes. The system should facilitate the formal sharing of lessons learned and trends identified during site visits for all phases of DFC's investment decision-making.
- **Recommendation 10:** Conduct an internal workforce assessment of the Office of Development Policy to determine the appropriate current and future staffing needs and budget resources to perform site visit monitoring to assess Environmental and Social compliance and development impact.
- **Recommendation 11:** Develop a system to track all significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments.

- **Recommendation 12:** Report significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments to DFC's Board of Directors and report such incidents in the Annual Report.
- **Recommendation 13:** Revise relevant policies and procedures to better define how significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments impact DFC's monitoring site visit priorities, annual plans, and/or schedule.

Photo 1: Top left photo-of a solar panel farm located in Northern India; Right photo: image of Mumbai skyline and the Dhobi Ghat, one of the world's largest outdoor laundry facilities; Bottom left photo: project auditor (r) and owner of a cement company (l) who obtained a micro finance loan.

MEMORANDUM:

Date: November 13, 2023

To: MR. SCOTT NATHAN
CHIEF EXECUTIVE OFFICER (CEO)

From: Mr. Anthony "Tony" Zakel.
Inspector General, Office of Inspector General

Subject: Draft Report – DFC Can Improve Oversight of Renewable Energy and Financing Projects in India (Audit Report DFC-24-002-C)

We contracted with the independent public accounting firm of RMA Associates, LLC's (RMA) to audit DFC's renewable energy and financing projects in India. The contract included reporting on (1) whether DFC involved the U.S. private sector and supported local country development in alignment with its mission; (2) assessing the inputs, data, and analyses used to assess and approve the projects; and (3) assessing the process and internal controls DFC used to identify and mitigate certain risks. The contract required that the audit be performed in accordance with U.S. generally accepted government auditing standards (GAGAS).

In its audit of DFC, RMA concluded that DFC supported local country development in alignment with its mission. However, DFC did not adequately support a waiver of environmental and social standards for one of the projects reviewed, resulting in $54.91 million in unsupported questioned costs. DFC also has not developed sufficient internal controls to support the approval process for projects financed through subordinated debt. In addition, DFC's records management system can be unreliable when compiling a complete set of documents for individual projects. Finally, DFC has not developed a risk-based assessment to determine which sites to visit or a method to track, report and monitor significant environmental and social events, particularly fatalities and serious injuries. Three fatalities and two serious injuries occurred on one of the reviewed projects.

In connection with the contract, we reviewed RMA's report and related documentation and inquired of its representatives. Our review, as differentiated from a performance audit of DFC's renewable energy and financing projects in India in accordance with GAGAS, was not intended to enable us to express, and we do not express, opinions or conclusions on whether DFC can improve oversight of its renewable energy and financing projects in India. RMA is responsible for the attached auditor's report dated November 13, 2023, and the conclusions expressed therein. However, our review disclosed no instances where RMA did not comply, in all material respects, with GAGAS.

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact me at 202-938-7986.

Anthony "Tony" Zakel
Inspector General
U.S. International Development Finance Corporation

CC: Scott Nathan (Chief Executive Officer)
Nisha Desai Biswal (Deputy Chief Executive Officer)
Jane Rhee (Chief of Staff)
Tina Donbeck (Chief Information Officer)
Jody Myers (Chief Risk Officer)
Larry Sacks (Chief Development Officer)
All Vice Presidents
Bill Kennedy (Director of Accountability)
Ryan Zalaskus (Managing Director, Internal Controls)
RMA Associates

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RMA | Associates
Auditors. Consultants. Advisors.

U.S. International Development Finance Corporation (DFC)

DFC Can Improve Oversight of Renewable Energy and Financing Projects in India
Order No: 140D0422F0138

Date: November 13, 2023

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November 13, 2023

Anthony "Tony" Zakel, Inspector General
Office of Inspector General
U.S. International Development Finance Corporation

Dear Mr. Zakel,

RMA Associates, LLC (RMA) is pleased to submit this performance audit report of U.S. International Development Finance Corporation's (DFC) renewable energy and financing projects in India in accordance with generally accepted government auditing standards (GAGAS, also known as the "Yellow Book").[4] Information on our findings and recommendations is included in the accompanying report.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We very much appreciate the opportunity to serve you and will be pleased to discuss any questions you may have.

Sincerely,

RMA Associates

RMA Associates, LLC
Arlington, VA

[4] Government Accountability Office Government Audit Standards (2018 Revision).

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Background

Photo 2: Located in Mumbai, the Gateway to India (right) stands next to the Taj Mahal Palace and Tower Hotel (left) overlooking the Arabian Sea.

The U.S. International Development Finance Corporation (DFC) is America's development finance institution. DFC is authorized by the Better Utilization of Investments Leading to Development Act of 2018 (BUILD Act) and began operations in January 2020. DFC assumed the functions of the Overseas Private Investment Corporation (OPIC) and the U.S. Agency for International Development's (USAID) Development Credit Authority (DCA). DFC uses financial tools to promote private investment in economic development with a focus on low and lower-middle income countries. It aims to support development impact, U.S. economic interests, and U.S. foreign policy. DFC must also consider, in its financing operations, the economic and financial soundness and development objectives of the projects for which it provides support.

Under the BUILD Act, DFC inherited OPIC's and DCA's authorities to offer direct loans, loan guaranties, and political risk insurance, and acquired additional authorities to offer equity investments and technical assistance. DFC has a maximum contingent liability of $60 billion, and a total projected exposure of $35.4 billion as of June 2023. In addition to prioritizing low and lower-middle income countries, DFC should give preference to projects involving U.S. persons as project counterparties or participants, as well as preference for support in countries complying with international trade obligations and embracing private enterprise. Projects must consider factors relating to environmental and social impact, worker rights, and human rights, among other considerations. DFC seeks to complement, and not compete with, the private sector.

DFC Financing Tools

To accomplish its mission, DFC is authorized to provide support through the following key financing tools.

- *Direct loans and loan guaranties* of up to $1 billion for terms between 5 and 25 years, subject to Federal credit law and other requirements, for investment projects and funds. DFC can provide direct loans to clients who lack a funding source of their own. DFC disburses funds directly from the U.S. Treasury and lends them to an eligible borrower.

  DFC can also provide loan guaranties to clients that have an independent funding source or are themselves independent funding sources (e.g., financial institutions) but are unable to provide funding without the risk mitigation DFC offers. These parties share the risk, accepting a risk of loss of at least 20 percent of the guaranteed support.

- *Equity investment* in specific projects or *investment funds*, with exposure limited to no more than 30 percent per project and 35 percent of overall DFC exposure. Per the BUILD Act, to use equity financing, the project must: 1) address a market failure; 2) include commercial partners; 3) promote significant developmental impact; and 4) be commercially sustainable.
- *Political risk insurance* coverage of up to $1 billion against losses due to political risks (e.g., currency inconvertibility, expropriation, and political violence), and *reinsurance* to increase underwriting capacity. DFC offers insurance to investors when private insurance is not available to make the investment viable. DFC generally requires the insured and its affiliates to bear the risk of loss for at least 10 percent of the amount of DFC's exposure.
- *Feasibility studies* and *technical assistance* to support project identification and preparation. DFC must aim to require cost-sharing by those receiving funds.

DFC

Financing Tools

Direct Loans

Loan Guaranties

Equity Investments

Investment Funds

Political Risk Insurance

Feasibility Studies

Technical Assistance

Source: www.dfc.gov

Development Impact

DFC uses a quantitative assessment tool, the "Impact Quotient" (IQ), to measure development impact. Based on the IQ score, projects are rated as *exceptionally impactful*, *highly impactful, impactful, limited impact,* or *indeterminate*.[5] The IQ score captures information related to three major categories: *economic growth, innovation,* and *inclusion.* Economic growth measures the project's potential for expanding economic activity. Innovation measures the project's potential to develop or scale new techniques and products. Inclusion measures the project's potential benefits to unrepresented or underserved people. IQ scores are intended to be measured and updated throughout the project life cycle.

Investing in India

This audit focused on DFC's renewable energy and financing projects in India, which is DFC's largest country investment partner at approximately $3.16 billion. There are 100 active DFC projects supporting the development of the world's most populated country, India, and its 1.4 billion citizens. These investments include, but are not limited to, renewable energy, finance, agriculture, insurance, health care, and manufacturing.

[5] These five tiers were effective beginning the fiscal year 2023. Prior to fiscal year 2023, there were three tiers: highly developmental, developmental, or indeterminate.

Why Conduct This Audit and Objectives

U.S. House of Representatives Report 116-444, State, Foreign Operations, and Related Programs Appropriations Bill, 2021 (HR Report 116-444), mandated that DFC Office of Inspector General (OIG) submit a report to the Committees on Appropriations assessing the integration and efficiency of DFC policies, procedures, and processes. Additionally, the Committees expressed interest in DFC OIG completing a follow-up audit similar to USAID OIG's audit of OPIC's Chile Energy Sector Portfolio that was completed in 2019.[6]

We also coordinated with DFC's Office of Accountability, an independent office within DFC that addresses concerns, complaints, or conflicts about environmental or social issues that may arise around DFC-supported projects. The Office of Accountability provides project-affected communities, project sponsors, and project workers an opportunity to have concerns independently reviewed and addressed. DFC's Board of Directors, in accordance with the BUILD Act, established the Office of Accountability as DFC's Independent Accountability Mechanism. It serves to improve the Corporation's effectiveness in fulfilling its mission by ensuring compliance with DFC requirements and enhancing information flow between locally impacted communities, project sponsors, and decision-makers. DFC also expects to benefit from the independent advice that the Office of Accountability will be able to provide. In 2018, DFC's predecessor, OPIC, issued an internal report prepared by the Office of Accountability assessing whether the use of client-reported data, supplemented by selected site visit monitoring, was adequate in achieving program goals.[7] This assessment was conducted in response to a 2015 U.S. Government Accountability Office (GAO) audit that noted concerns with the agency's monitoring of Environmental and Social (E&S) compliance and its reliance on client-reported data, which can be inaccurate or incomplete.[8] The internal report found that the client-reported data examined was of "dubious quality" but, in the absence of site visits, was the only formal mechanism to obtain E&S information from every project financed. Furthermore, it concluded that client-reported data was inadequate to assess E&S compliance as outlined in the agreement terms.

This audit focuses on DFC's renewable energy and financing projects in India, which is a major strategic investment partner for DFC. The U.S. government signed an Investment Incentive Agreement on May 23, 2022, with the Government of India (GoI) to encourage economic activities that promote the development of the economic resources and productive capacities in India. The Agreement acknowledges that private-sector investment can contribute to India's economic goals.

This audit had three objectives, drawn directly from the previous USAID OIG report on OPIC's work in the Chile energy sector. The objectives of this audit were:

- determine if DFC involved the U.S. private sector and supported local country development in alignment with its mission;
- assess the inputs, data, and analyses used to assess and approve the projects; and
- assess the process and internal controls DFC used to identify and mitigate certain risks.

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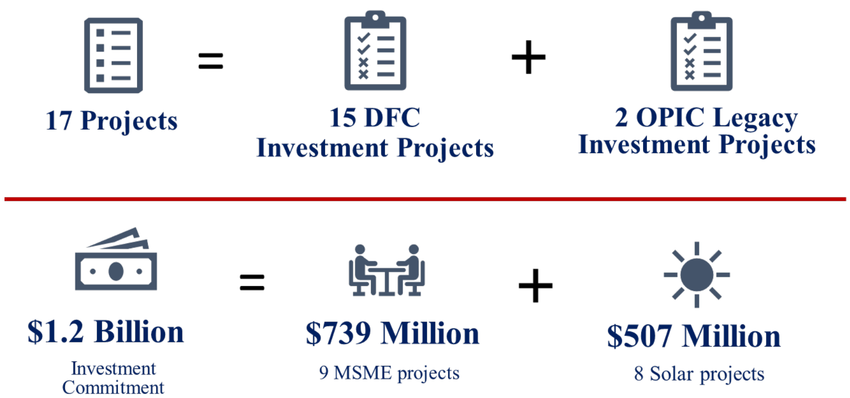
[6] Office of Inspector General, U.S. Agency for International Development, "OPIC Investments Increased Chile's Energy Capacity, but Weak Processes and Internal Controls Diminish OPIC's Ability to Gauge Project Effects and Risks," February 1, 2019, Audit Report No. (9-OPC-19-002-P), p. 9.
[7] OPIC's Office of Accountability, *Assessment of OPIC's Environmental and Social (E&S) Monitoring of Projects*, February 7, 2018, p. 63.
[8] GAO, "Overseas Private Investment Corporation, Additional Actions Could Improve Monitoring Processes", December 2015, Report No. (GAO-16-64), p. 34-39.

The audit focused on a sample of 15 active DFC investment projects and two OPIC legacy investments in India (See Picture 1, a map of the locations the audit team visited and **Appendix II: Summary of Sampled Investments**). These sample projects represent a DFC commitment[9] of over $1.2 billion. The investments include eight renewable energy projects with a commitment total of $507 million, and nine micro, small, and medium enterprise (MSME) projects with a commitment total of $739 million. The projected private capital mobilization for the 17 projects we reviewed is approximately $1.4 billion (53 percent private industry and 47 percent DFC).

Graphic 1: Highlights of the sampled projects the audit team reviewed.



[9] The commitment is the total not to exceed principal amount of a loan to a counterparty.

Graphic 2: Map of Solar Plants and Microfinance Lender Locations the Audit Team Visited.

EXAMPLE OF DEVELOPMENT IMPACT FOR RECIPIENT OF VEHICLE FINANCING LOAN

DFC's $250 million loan to an Indian company specializing in pre-owned vehicle financing has had a powerful impact for many of those receiving such loans. The audit team met with one such individual who was able to purchase a pre-owned vehicle.

The gentleman told the team that before purchasing the vehicle he worked as a mechanic. He used the loan to start his own business and currently uses the vehicle for ridesharing and as a tourist vehicle.

Additional vehicle loans from this investment have been used by other entrepreneurs to start new businesses. Vehicle ownership loans empower individuals by giving them greater economic mobility and freedom while also giving small enterprises a credit line to expand operations.

Audit Findings

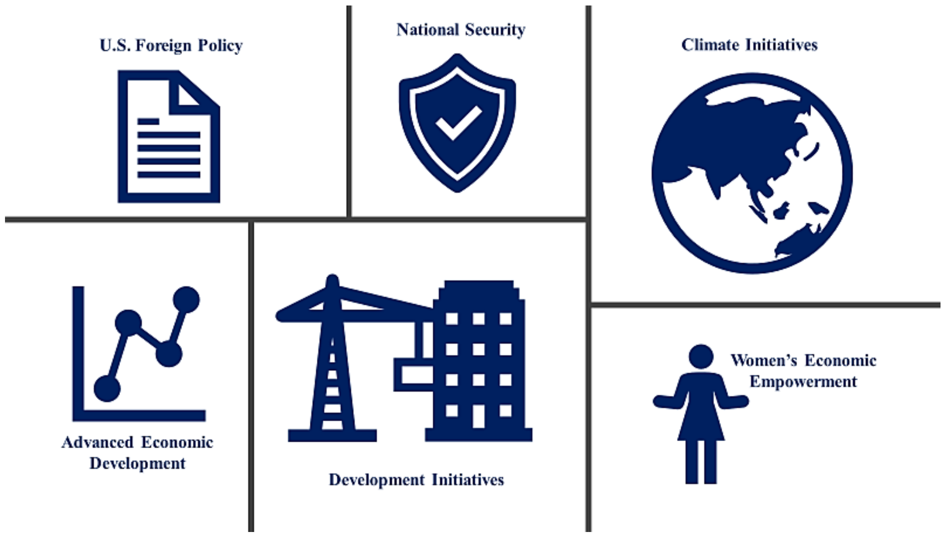
Our audit determined DFC supported local country development in alignment with its mission and BUILD Act requirements regarding project counterparty considerations. However, we determined DFC needs to improve records management, develop stronger policy around the use of subordinated debt, improve compliance and development impact monitoring, and implement better monitoring, tracking, and reporting of significant environmental and social events, including fatalities and serious injuries. We made 13 recommendations to improve DFC's strategic approach to advancing its mission and strengthening its internal control system. See Appendix I for our methodology addressing the objectives, and for recommendations refer to **Summary of Recommendations and Management Comments**.

DFC Supported Local Country Development in Alignment with Its Mission and BUILD Act Requirements Regarding Project Counterparty Considerations

DFC has facilitated business investments in the Indian markets to strengthen the U.S. – India relationship and improve trade between the two countries. We determined that the 17 projects we reviewed aligned with DFC's mission and foreign policy objectives. Specifically, the projects complemented USAID/India's Country Development Cooperation Strategy (CDCS) and focused on renewable energy and increased lending to MSMEs, as previously mentioned. These efforts are in alignment with the U.S. government's foreign policy objectives in India to increase renewable energy capacity and distribution. Transactions with financial intermediaries, especially in the MSME sector, also contribute towards economic goals and strategies, while many also support women's economic empowerment. OPIC was required to involve U.S. private sector organizations; however, that requirement was lifted under the BUILD Act, which allows DFC to involve others beyond the U.S. private sector.

Finding #1: DFC Aligned Investments with Its Mission and U.S. Foreign Policy Objectives in India

The BUILD Act requires DFC to facilitate market-based, private-sector development and inclusive economic growth in less developed countries.[10] DFC's investments work to complement and mobilize private sector capital into projects that advance economic growth, development, and poverty reduction. Projects should also align with U.S. foreign policy and national security objectives.



Graphic 3: DFC investments aim to support development, foreign policy, and national security initiatives.

Climate Initiatives

In January 2021, President Biden signed Executive Order (EO) 14008, "Tackling the Climate Crisis at Home and Abroad". This EO placed the climate crisis at the center of U.S. foreign policy and national security.[11] It called for the DFC Chief Executive Officer, along with the heads of other Federal agencies and partners, in consultation with the Assistant to the President for National Security Affairs, to identify how the U.S. can promote ending international financing of carbon-intensive fossil fuel-based energy and advance sustainable development. In response to this, DFC developed a Climate Action Plan, outlining how the corporation will transition its approach to climate finance. The plan prioritizes DFC's investments in climate resistant projects and the mobilization of private capital to maximize impact and minimize risk.

To further these foreign policy objectives, the U.S. and Indian governments announced the U.S.-India Climate and Clean Energy 2030 Partnership in April 2021. Its purpose was to accelerate progress towards shared climate and clean energy goals. In September 2021, the partnership was further strengthened by the launch of four clean energy partnership pillars focusing on responsible oil and gas, energy efficiency, renewable energy, and sustainable growth. The goals outlined in the renewable energy pillar call for supporting India to achieve its 450 gigawatts renewable energy target by 2030, expanding the use of distributed renewables, and strengthening the relationship and trade ties between the two countries. Under this pillar, DFC's commitment to providing $415 million in loans for five solar energy projects contributing

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[10] BUILD Act Section 1411.
[11] Executive Order 14008, "Tackling the Climate Crisis at Home and Abroad," Part 1, p. 1 (EO 14008).

855 megawatts (MW) of renewable energy was cited as a key achievement.[12] The eight renewable energy projects in the audit align with these foreign policy goals.

Development Initiatives

In conjunction with U.S. foreign policy objectives, the BUILD Act requires DFC's Chief Risk Officer (CRO) to work with the USAID Administrator to pursue projects that complement USAID's CDCS, and by extension the Department of State's Joint Strategic Plan.[13] USAID/India's 2020-2024 CDCS stated goal is "India Accelerates its Own Inclusive Development and Fosters Enhanced Regional Connectivity." It calls for USAID projects in India to work towards contributing to three development objectives, including efforts to reduce pollution and cross-cutting themes of inclusive development, gender, and private sector engagement. The 17 projects reviewed in this audit complemented USAID/India's CDCS through their focus on either renewable energy or increased lending to MSMEs, including those owned by women.

Women's Economic Empowerment

The BUILD Act also requires DFC to prioritize women's economic empowerment.[14] DFC meets this objective by investing in projects owned and led by women, as well as projects that provide a product or service that empowers women. DFC uses criteria established by the 2X Challenge to assess whether a potential project supports women.[15] Six of the 17 projects selected in this audit were aligned with the 2X Challenge criteria through increased lending to female MSME entrepreneurs or increased female employment within the counterparty's organization.

Advance Economic Growth

Private capital mobilization is a measurement of economic activity generated outside the non-official sector as the result of official sector investment operations. Multilateral development banks have defined private capital mobilization as including both private direct and indirect mobilization, counting investments by private entities established for business purposes with both financial and managerial autonomy. The projected private capital mobilization for the 17 projects we reviewed is approximately $1.378 billion.

We determined that the 17 projects in our sample aligned with DFC's mission and foreign policy objectives. Specifically, the projects complemented USAID/India's CDCS and focused on renewable energy and increased lending to MSMEs, as previously mentioned.

Finding #2: DFC Met BUILD Act Requirements Regarding Project Counterparty Considerations

DFC's predecessor, OPIC, was required by statute to include the U.S. private sector in all projects financed by the corporation.[16] To meet this U.S. participation requirement, OPIC policy stated that a U.S. company must hold a minimum of 25 percent of equity, or the equivalent value, in a project. A 2018 audit conducted by USAID OIG found the corporation to be compliant with this requirement. The BUILD Act encourages, but does not require, DFC to provide preferential consideration to projects involving U.S. citizens.[17] The

[12] 855 MW has the capacity to power over 700,000 American homes, per the U.S. Energy Information Administration's information on average U.S. residential electricity consumption.
[13] BUILD Act Section 1445(a)(5).
[14] BUILD Act Section 1451(f).
[15] The 2X Challenge was launched at the Group of 7 Summit in 2018 to inspire development financial institutions, international financial institutions, and the private sector to invest in women (https://www.2xchallenge.org/).
[16] The Foreign Assistance Act of 1961, Section 231, as amended, codified in Title 22 of the United States Code (U.S.C.), Section 2191.
[17] BUILD Act Section 1451(b)(1).

BUILD Act also gives preference for DFC to work in countries whose governments demonstrated consistent support for economic policies that promote private enterprise development.[18] DFC has assessed India as a country whose government meets this preference. Furthermore, a DFC policy directive states that it will provide preferential support to entities that are majority-owned or controlled by private sector entities, except for support provided to qualifying sovereign entities.[19] The 17 DFC projects in our sample met these qualifying preferences.

Inputs, Data, and Analysis Used to Assess and Approve Projects Are Adequate, But Improvements Can Be Made

DFC uses a variety of inputs, data, and systems to analyze, assess, and approve projects. These include systems to manage internal documents; internal policies, procedures, and directives; clearance reports; approval thresholds; and finance agreements. While these all form a critical foundation and structure, we identified three areas where project assessment and approval processes were not adequate. First, DFC did not adequately support the waiver of Environmental and Social Policy and Procedures (ESPP) on a project with an Indian counterparty, which resulted in $54.91 million in unsupported questioned costs. Second, DFC has not developed sufficient internal controls to support the approval process for projects financed through subordinated debt. Third, DFC's records management system can be unreliable in compiling a complete set of documents for individual projects.

Graphic 4: Information is collected to support each project and end users relay on this information to evaluate and approve projects and ensure the project meets agreed upon requirements.

Finding #3: DFC Did Not Adequately Support a Waiver of Environmental and Social Policy Standards Resulting in $54.91 million in Unsupported Questioned Costs

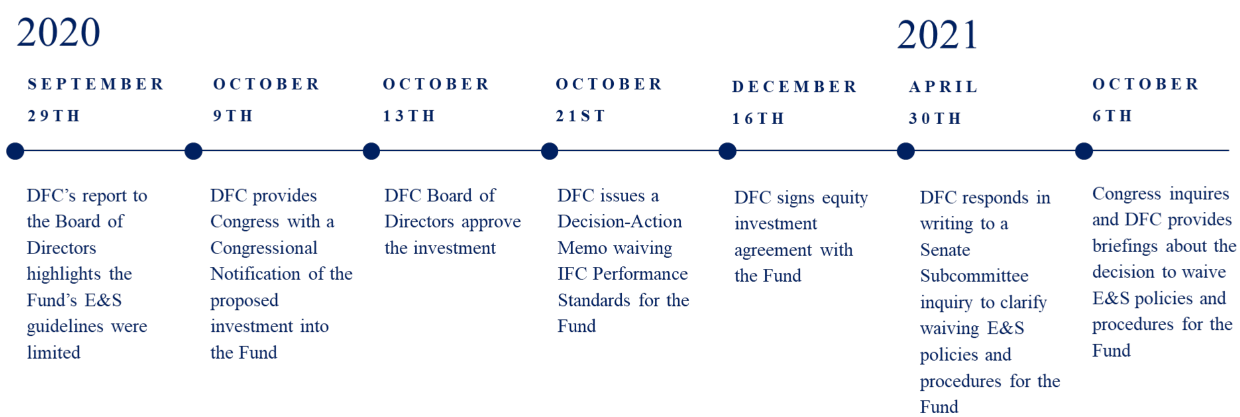
DFC's authorizing statute directs DFC to "provide countries a robust alternative to state-directed investments by authoritarian governments and United States strategic competitors using best practices with respect to transparency and environmental and social safeguards."[20] DFC has implemented this mandate by requiring supported projects to comply with DFC's ESPP and applicable provisions of the International Finance Corporation's (IFC) Performance Standards on Social and Environmental Sustainability (Performance Standards), which are incorporated in the ESPP by reference.[21] The IFC Performance Standards provide guidance on how to avoid, manage, and mitigate environmental and social risks and impacts so that development opportunities are enhanced and sustainable. They provide best practices in

[18] BUILD Act Section 1451(g).
[19] DFC Other Investment Preference and Policy Requirements Directive, PD-010, dated February 28, 2022. This Directive also states the term "qualifying sovereign entities" to be any agency or instrumentality of a foreign state that has a purpose that is similar to the purpose of the Corporation as described in section 22 of the U.S.C. § 9612(b); or (2) any international financial institution.
[20] BUILD Act Section 1441 (6).
[21] DFC Environmental and Social Policy and Procedures dated July 2020.

areas such as labor and working conditions, pollution prevention, health and safety, land acquisition, biodiversity conservation, indigenous populations, and cultural heritage.[22]

We found DFC did not adequately support a waiver of environmental and social policy standards for its equity investment in Renewable Energy Project No. 4 (the Fund)[23] and instead allowed the Fund to use less stringent provisions of Indian law. As a result, we identified $54.91 million in unsupported questioned costs. The timeline below depicts the process used to approve the deal.

On October 21, 2020, DFC Management stated that it waived these standards because the investment was "highly aligned with U.S. foreign policy interest" allowing an opportunity to support India's critical energy needs. By waiving IFC Performance Standards, DFC undermined its BUILD Act mandate to adhere to best practices concerning environmental and social safeguards. Requiring adherence to IFC Performance Standards is critical, as the majority of countries DFC invests in are low-income and lower-middle income countries, which oftentimes lack strong government and judicial systems to enforce workers' rights, human rights, and environmental regulation.



Graphic 5: Event timeline outlining DFC's waiver of Environmental and Social Policies and Procedures.

On December 16, 2020, DFC signed an equity investment agreement with the Fund for $54,910,000. For this investment, DFC waived its required ESPP and allowed the Fund to use less stringent provisions of Indian law.

The Fund is 51 percent owned by institutional investors and 49 percent owned by the GoI. The Fund Manager informed DFC that because the Fund was a quasi-sovereign entity, a waiver of IFC Performance Standards was necessary as it would only require compliance with Indian national law and applicable state and local laws. DFC Management was aware that the Fund's E&S Guidelines were less protective than IFC Performance Standards. DFC Management's report on the Fund's equity investment, dated September 29, 2020, to DFC's Board of Directors stated the following:

> *"The Project has a [high][24] E&S Risk Deduction because the Fund does not apply International Best Practice (defined as the IFC Performance Standards) to downstream investments; the Fund's E&S management capacity is limited at this time; the Fund will be heavily dependent on joint venture*

[22] IFC Performance Standards on Environmental and Social Sustainability, January 1, 2012.

[23] See Appendix II for a list of all eight renewable energy projects and all nine financial intermediary projects included in the audit scope.

[24] While DFC's report stated "medium," in their subsequent discussion with the Board, Management stated this was an error and should have stated "high."

> *partners for implementation; national-level enforcement of E&S regulations may be weak; and as a first-time Fund manager, the Fund does not have an E&S track record. Infrastructure projects have the potential for significant environmental and social impacts."*

DFC Management also informed the Board that the Fund's final close was scheduled on October 26, 2020; thus, DFC needed to complete all internal approvals and execute committing documents prior to that date. The Board approved DFC's investment in the Fund on October 13, 2020.

On October 21, 2020, DFC issued a Decision-Action Memorandum waiving compliance of the following ESPP sections for DFC's investment in the Fund:[25]

- §2.9 – Requirement that all applicants meet the requirements of the Performance Standards.
- §3.4 – DFC will incorporate the Performance Standards that the project is required to meet in DFC agreements.
- §3.6 – Projects that are not expected to meet the requirements of the Performance Standards will be declined.
- §§3.7, 3.9, 8.12 – Applicants must meet the Performance Standards and have an ESMS that meets the requirements of the Performance Standards.
- §3.32 – Where the Performance Standards are more stringent than host country law, financial intermediaries shall apply the Performance Standards.

The Decision-Action Memorandum's justification for waiving these ESPP sections was that the Fund's investment was "highly aligned with U.S. foreign policy interests," presenting an opportunity for DFC to partner with the GoI by providing financial support for India's critical energy and other core infrastructure development priorities.

Why is ESPP Important?

Environmental and Social Policy and Procedures (ESPP) exist to protect human and workers' rights as well as the environment.

On October 9, 2020, DFC provided Congress with a Congressional Notification regarding its proposed investment in the Fund. In the notification, DFC disclosed that the Fund was partially owned by the GoI. However, DFC did not state that it would have to waive compliance of IFC Performance Standards and instead rely on compliance with Indian national law and applicable state and local laws, which are less protective. Instead, DFC made the following statement:

"The Fund has an environmental and social policy (ESP) in place and has developed a set of E&S management principles. These management principles are similar to the IFC Performance Standards."

In an April 30, 2021, letter to Senator Chris Coons, Chair of the Senate Subcommittee on State, Foreign Operations, and Related Program, DFC explained that:

> *"[The Fund] has an Environmental and Social Policy in place and has developed a set of E&S management principles that will be used to guide the fund's investments. While [the Fund's] management principles are similar to the IFC Performance Standards, they are not fully aligned,*

[25] This memo also approved the use of Financial Intermediary Policy for Category A subprojects.

with weaknesses [in the Fund's principles] being identified in the areas of occupational health and safety, labor management, land acquisition and protection of vulnerable people."

On October 6, 2021, DFC received an inquiry from a staff member of the Senate Subcommittee on State, Foreign Operations, and Related Programs regarding DFC's authority to waive the Fund's environmental and social policies and procedures. That same day, DFC conducted a phone conversation with individuals from the House regarding the same issue. DFC officials formally responded to the congressional inquiry in writing as follows:

> *"DFC gave a blanket waiver to the Performance Standards.*[26] *DFC pointed to the high priority of the Indo-Pacific as a foreign policy priority and a critical region for DFC and stated that the investment presented an opportunity for DFC to partner with the Government of India and provide financial support for India's critical energy and other core infrastructure development priorities as reasons for granting the waiver."*

DFC also explained that the waiver was necessary due to "sovereignty issues" (i.e., the Fund's sovereign minority ownership). DFC officials informed Senate and House officials that moving forward, current DFC leadership would not support any future blanket waivers to the IFC Performance Standards such as those granted for DFC's investments in the Fund. DFC stated that current leadership is following "*past practice where narrowly tailored waivers were granted on a very rare basis.*" Consistent with this, DFC said future waivers would only be granted when the three following conditions are met:

- *The project represents an extraordinary opportunity to fulfill the DFC's mission as set forth in the BUILD Act.*
- *The waiver requested is to limited, specific, and well-defined aspects of the Performance Standards.*
- *After a rigorous evaluation with the input of relevant stakeholders, DFC has been unable to find technically and financially feasible alternatives to seeking a waiver to the applicable Performance Standard or Standards.*

On November 4, 2022, during our audit, DFC approved revisions to its Directive for Office of Development Policy (ODP). Among the revisions was a standard for waiving ESPP requirements. In a memorandum explaining the revised Directive, DFC stated that it will decline to proceed with projects not expected to meet the requirements of the IFC Performance Standards. DFC stated the IFC Performance Standards had been waived in limited ways twice and a blanket waiver from the IFC Performance Standards once (i.e., the Fund's equity investment).[27] The memorandum went on to state future waivers would only be granted on an infrequent basis when the three conditions listed above were met.

DFC's justification for approving the blanket waiver of ESPP pertaining to IFC Performance Standards for DFC's investment in the Fund was that the investment was highly developmental and aligned with U.S. foreign policy interests. However, these conclusions could be stated for almost all DFC investments in India and other countries. And while the Fund required DFC to waive IFC Performance Standards as a condition of its investment in the Fund, it was only after DFC received inquiries from Congressional staff, and our audit was on-going, that DFC enacted its limited waiver policy.

[26] DFC waived adherence to the IFC Performance Standards but did not waive its requirements related to protecting worker's rights.
[27] DFC's past two limited waivers to IFC Performance Standards related to an investment in a combined-cycle thermal power plant in Senegal in 2015 and 2016. The waivers were narrowly tailored to address specific particulate stack emissions requirements under the development of the plant.

DFC undermined its BUILD Act mandate to adhere to environmental and social safeguard best practices.

By waiving IFC Performance Standards, DFC undermined its BUILD Act mandate to adhere to best practices concerning environmental and social safeguards. Requiring adherence to IFC Performance Standards is critical, as the majority of countries DFC invests in are low-income and lower-middle income countries, which oftentimes lack strong government and judicial systems to enforce workers' rights, human rights, and environmental regulation. For example, the State Department's 2022 Human Rights Report on India documented cases of interference with the freedom of peaceful assembly and freedom of association; existence of forced and compulsory labor; crimes involving violence or threats of violence targeting members of national/racial/ethnic and minority groups based on religious affiliation; and serious government harassment of domestic and international human rights organizations. Further, while the blanket waiver did not include a waiver of the worker's rights standards, DFC's internal environmental and social assessment of the investment in the Fund identified concerns related to the regulatory environment and its ability to manage downstream investment performance with respect to land acquisition, stakeholder engagement, workforce protections, and the recognition of rights for indigenous peoples to be of greatest concern. And as detailed in this report, the Fund has reported three fatalities and two serious injuries occurring on separate project sites (see **Appendix IV: Summary of Significant Environmental and Social Events**). We further believe that any future waivers of ESPP standards should also be evaluated by the CRO, and coordinated with the Office of Accountability, whose role is to address concerns, complaints, or conflicts about environmental or social issues that may arise around DFC-supported projects. For these reasons, DFC should ensure the three conditions outlined in the Front Office Memo on Environmental and Social Policy and Procedures are incorporated into policy, and ensure any future limited waivers are fully supported with appropriate documentation, rationale, and disclosed as part of the congressional notification process.

$54.91 Million of DFC's Investment in Renewable Energy Project No. 4 Is Deemed Unsupported Questioned Costs

The Inspector General Act of 1978, as amended (IG Act),[28] defines unsupported questioned costs as "a finding that, at the time of the audit, the cost is not supported by adequate documentation."[29] As detailed above, at the time of the Fund's waiver DFC did not have policies and procedures to grant waivers of the ESPP. DFC modified Directive OD-004 in January 2023 to state:

"Under the ESPP, the Corporation will decline to proceed with projects that are not expected to meet the requirements of IFC Performance Standards. Limited waivers to the Performance Standards are only granted on an infrequent basis when:

1) the project represents an extraordinary opportunity to fulfil the DFC's mission as set forth in the BUILD Act;
2) the waiver requested is to limited, specific, and well-defined aspects of the Performance Standards; and
3) after a rigorous evaluation with the input of relevant stakeholders DFC has been unable to find technically and financially feasible alternatives to seeking a waiver to the applicable Performance Standard or Standards."

[28] 5 U.S.C. Ch. 4.
[29] 5 U.S.C. § 405(a)(4)(B).

Because the above policy directive was enacted during the audit, we are not making a recommendation regarding the development of policy and criteria regarding waivers in this report.

The rationale provided by DFC for the waiver of the ESPP – that the project was a highly developmental project aligned with foreign security goals – could be stated for many projects that DFC supports and is not unique to the Fund. Further, DFC's waiver of the IFC Performance Standards for the investment in the Fund does not meet any of the three newly stated requirements. Therefore, we consider the $54.91 million investment in the Fund to be unsupported questioned costs under the IG Act.

For the waiver of Environmental and Social Policy and Procedures, see recommendations 1-2 in the **Summary of Recommendations and Management Comments**.

Finding #4: DFC Has Not Developed Sufficient Internal Controls to Support the Approval Process for Projects Financed Through Subordinated Debt

One of DFC's financing tools provides direct loans to counterparties. In the event the counterparty should experience financial difficulties and face either bankruptcy or liquidation, the priority in which DFC would be repaid depends on the terms of the loan agreement. Loans classified as "senior debt" are prioritized for repayment ahead of loans classified as "subordinated debt." Thus, subordinated debt inherently carries a higher risk that the investment will not be repaid. The BUILD Act acknowledges this risk by stating that any loan or loan guaranty made by DFC should be on a senior basis (or *pari passu*[30]) with other senior debt unless there is a substantive policy rationale to support such a project.[31]

> **What is Subordinated Debt?**
>
> Subordinated debt is any type of loan that's paid after all other senior debts and loans are paid, should the borrower default. Subordinated debt is riskier.

DFC has not developed specific policies on when using subordinated debt is appropriate; enhanced approval processes surrounding these types of loans; or developed specific risk mitigation procedures or tools to ensure the risks associated with the use of subordinated debt are fully considered and evaluated within DFC's Enterprise Risk Management (ERM) process. DFC's Loan and Guaranty Directive is the only guidance the Corporation has concerning subordinated debt, and the directive's focus is on senior debt.[32] Moreover, the Directive only states when the use of subordinated debt is justified, which includes the achievement of a specific development or foreign policy objective of the U.S. government, the alleviation of a credit market imperfection, or to ensure the economic viability of a project. The policy does not include a discussion on when using subordinated debt is appropriate; any enhanced approval processes surrounding these types of loans; or specific risk mitigation procedures or tools to ensure the risks associated with the use of subordinated debt are fully considered and evaluated within DFC's ERM process.

DFC officials who were interviewed stated a specific policy on subordinated debt is not necessary because the policy rationale is determined at the project level, either through the investment committee, management, or board clearance, depending on the size of the loan. Furthermore, DFC officials said loans classified as subordinated debt are rarely used. We found that DFC's worldwide portfolio contains 12

[30] "*Pari passu*" is a Latin phrase meaning "equal footing." In the context of finance, it means that two or more parties to a financial contract or claim are treated the same and paid in equal rank.
[31] BUILD Act Section 1422(b)(12).
[32] Loan and Guaranty Directive, PD-001, effective January 1, 2020.

projects, including two in India, classified as subordinated debt. These subordinated debt projects totaled approximately $926 million out of DFC's $35.4 billion (or 2.6 percent) of projected exposure as of June 2023. Finalizing the "Standards for Assessing the Credit Risk of New Loans and Guaranties" relating to subordinated debt will allow DFC to set out more specific guidance that is not included in the Loan and Guaranty Directive. Such guidance could include the approval thresholds for subordinated debt loan agreements, the types of loans that are best aligned to the policy grounds for junior or mezzanine debt laid out in the Directive, and the specific financial, environmental, and social protections to be used in the subordinated debt loan agreements.

While subordinated debt financing carries a higher risk of loss, DFC believes that such projects also allow it to achieve greater development impact goals. Subordinated debt may greatly assist the counterparty by lowering its cost of capital, allowing it to work in market segments that would otherwise not be feasible. For example, a bank or financial intermediary receiving a subordinated loan from DFC would then have the market capital and capacity to provide small business loans to women or other disadvantaged groups. These loans in turn assist such groups in achieving their business goals, ultimately delivering greater developmental impact. And while DFC's current use of subordinated debt is small in relation to its total portfolio, as the Corporation grows, its use of subordinated debt may expand.

The Office of Management and Budget (OMB) Circular No. A-123 states that Federal agencies should have appropriate management systems and processes in place to ensure risks are identified early, brought to leadership's attention, and solutions are developed.[33] DFC's Office of the Chief Risk Officer (OCRO) oversees the ERM process, which addresses OMB Circular A-123 requirements. The OCRO can assess how best to identify, manage, and mitigate risks associated with subordinated debt at the enterprise level. By more completely embedding subordinated debt usage into DFC's ERM process, DFC will benefit from tools and resources to better identify, manage, and mitigate risk and protect taxpayer's dollars.

For DFC's use of subordinated debt, see recommendations 3 and 4 in the **Summary of Recommendations and Management Comments**.

Finding #5: DFC's Records Management System Can be Unreliable in Compiling a Complete Set of Documents for Individual Projects.

Image 1: Documents converted into electronic format.

DFC uses several different database systems to store project information and documentation. The two primary systems used by DFC are Content Manager and Insight. Content Manager is DFC's official Federal records system containing key final project documentation. Insight is DFC's project record system that shows project approval workflows and clearances, as well as other applicable project documentation. When DFC officials upload certain documents into Insight, the system is designed to automatically upload the applicable documents into Content Manager. However, we found that the two systems do not interface properly, and certain required documents were missing in Content Manager for all 17 projects we

[33] OMB Circular No A-123 "Management's Responsibility for Enterprise Risk Management and Internal Control", July 15, 2016 (M-16-17).

reviewed, such as finalized clearance and agreement documents. When a DFC official uploads key final project documentation into Insight, it is not always automatically loaded into Content Manager as designed and required. Likewise, if a DFC official uploads key final documentation directly into Content Manager, that information is not captured by Insight. Instead, the documentation must be separately uploaded into Insight. DFC officials have been aware for several years that Content Manager does not easily integrate with other databases, and this issue has not been resolved. Without adequate controls and interfaces to ensure all appropriate documents are properly transmitted from Insight to Content Manager (which is the official Federal records system), users have difficulty identifying which documents within the system are the finalized and approved documents that followed the appropriate workflows.

For records management, see recommendations 5 and 6 in the **Summary of Recommendations and Management Comments**.

Client Protection Principles

Throughout the audit, we did not identify any issues regarding customer over-indebtedness or harassment. Loan recipients we spoke with during the site visits did not disclose any problems or concerns with payment or collection practices. The financial intermediaries implemented credit checks to ensure customers do not become overburdened with debt, offered education to improve customers' financial literacy, and had mechanisms to address customer concerns in alignment with Indian regulations. The review, however, was limited to the financial intermediaries.

One company, by policy, sells its delinquent loans to collection agencies. Officials interviewed at the financial intermediary stated that the collections agencies were ethical and met the applicable legal standards of India. We did not meet with the collection agencies to review their practices as this was outside the scope of this audit. However, we may pursue this issue in a future audit to further address concerns expressed by members of Congress related to client protection principles. As part of its E&S clearance process, DFC has procedures in place to review the financial intermediaries' lending practices to ensure they have a grievance process in cases where a client believes they are being unfairly treated. DFC also encourages clients to conduct a self-assessment of their organization's client protection principles utilizing a free self-assessment tool.[34] DFC has also established a working group to develop recommendations regarding enhancements to their due diligence regarding client protection principles.

[34] DFC's Client Protection Resources.

DFC's Monitoring for Environmental and Social Compliance and Development Impact Needs Strengthening to Identify and Mitigate Risks

What are Client Protection Principles?

Client Protection Principles exist to protect borrowers from predatory lending and collection practices.

DFC has processes and internal controls to mitigate risks. Specifically, we noted controls are in place to address client protection principles. In addition, while we noted solar panels from Chinese sources were procured at several of the sites we visited, none we observed were from prohibited sources.[35] However, we learned that DFC officials did not visit Indian project sites where fatalities occurred and has no formal method for incorporating fatalities and serious injuries on a project site into its risk-based site visit determination process. Further, DFC's risk-based site visit methodology is not tied to strategic plans and goals for monitoring, focused on when DFC staff will make site visits, when third parties will be used for monitoring, and when no site visits are required. Finally, the budget for the Impact Management, Monitoring, and Learning (IMML) Division's staffing should be enhanced given its projected workload. These issues occurred because DFC is a new agency and had not identified the need to formalize strategic plans and goals for monitoring and believed the current risk-based monitoring plans met their needs. Further, management had not identified the need to conduct a formal internal workforce assessment of the resources needed to perform E&S compliance and development impact monitoring.

[35] Xinjiang Business Advisory, "*Risks and Considerations for Businesses and Individuals with Exposure to Entities Engaged in Forced Labor and other Human Rights Abuses linked to Xinjiang, China*," July 13, 2021; https://www.state.gov/wp-content/uploads/2021/07/Xinjiang-Business-Advisory-13July2021.pdf.

Finding #6: DFC Does Not Have Strategic Level Objectives, Plans, and Measurable Goals for Project Site Visit Monitoring

Photo 3: The top two photos represent solar fields with buried cables and well-groomed grounds. The bottom two photos represent solar fields with above ground cables and unkempt grounds, which can increase the potential for hazards.

OMB provides guidance on effective monitoring to Federal agencies that administer U.S. international assistance, such as DFC.[36] OMB states that monitoring should be planned early, sufficiently resourced, and shared. OMB further states that agencies should establish annual monitoring objectives and plans. This can be done centrally, or when decentralized agency policies should require that operating units annually document their monitoring objectives, plans, and include measurable goals. Additionally, DFC's Monitoring Directive states that the Chief Development Officer (CDO) will develop the monitoring and evaluation systems for development impact, implemented by ODP and other relevant offices.[37] Likewise, the CRO will establish the financial monitoring system, implemented by the Office of Finance and other relevant offices. It states that the CDO and the CRO will coordinate to develop a formalized process for capturing and disseminating positive and negative lessons learned from project monitoring and propose relevant policies and procedures accordingly.

DFC has not developed strategic level organizational objectives, plans, or measurable goals for site visit monitoring despite this OMB guidance and the critical importance of site visit monitoring. Furthermore, there is no formal process for DFC divisions to develop an annual site visit monitoring plan linked to strategic plans and goals. DFC's current site visit monitoring process at the division level is ad hoc, informal, and not driven by strategic goals. Divisions work independently from one another using a risk-based approach to determine what site visits they will conduct. However, we found most divisions were unable to provide us with a site visit plan for the current fiscal year (FY) and stated they were under development. Furthermore, there is only informal coordination between ODP and financial monitoring officials in conducting site visit work. For example, ODP monitoring officials responsible for environmental, social, and development impact work closely to select, plan, and conduct site visit work,

[36] OMB Monitoring and Evaluation Guidelines for Federal Departments and Agencies that Administer United States Foreign Assistance; January 11, 2018 (M-18-04).
[37] Monitoring Directive, PD-016, January 1, 2020, Section 2.

and reach out to financial monitoring officials to determine what, if any, site visits have been conducted for a particular project when travel planning is taking place.

Why are Site Visits Important?

Visiting DFC investments confirm if the objectives of the project are being met. Site visits also help to enhance relationships with partners.

DFC's strategic plan, goals, and measurable results for site visit monitoring should be publicly reported. For example, while DFC's FY 2021 annual report provided some information on site visits, the data was not clear, and did not set an overall strategic objective, or establish goals. Additionally, DFC reported a total of 34 E&S compliance monitoring actions in its FY 2021 Annual Report. However, it defined E&S compliance monitoring as being either physical or virtual to ensure compliance with project loan covenants.[38] Additionally, it did not provide any context as to how many E&S compliance monitoring actions were planned for that year against the reported results. Developing an overall strategic objective and publicly reporting annual site visit monitor plans, goals, and actual performance is critical to ensuring the various stakeholders, including Congress and the American public, are provided transparent information[39] regarding DFC's oversight of projects and the accomplishment of goals in this area.

While DFC Conducts Significant Due Diligence During the Origination Phase, DFC Needs to Strategically Plan and Improve Environmental & Social Compliance Project Site Monitoring and Development Impact Measurement

DFC performs a significant amount of up-front research and due diligence during what is referred to as the "origination phase" to determine the viability of a potential project. This involves an initial assessment performed by the deal's origination team; additionality determination;[40] subsidy calculation;[41] know-your-customer and due diligence checks; environmental, social, and economic clearances; development impact assessment;[42] congressional notification; and an informal Office of External Affairs review. Also, depending on the amount of support to the project, the credit committee, investment committee, and DFC Board of Directors must review and approve the deal.[43]

[38] DFC 2021 Annual Report, p. 80.
[39] BUILD Act 1411(6).
[40] DFC must ensure that its support of a project is "additional" to private sector resources by mobilizing private capital that would otherwise not be offered without such support.
[41] Under the Federal Credit Reform Act of 1990, agencies, including DFC, are required to estimate and request appropriations for the long-term costs, or subsidy costs, of their credit activities (Pub. L. No. 101-508, Title XIII, § 13201 (Nov. 5, 1990), codified at 2 U.S.C. §§ 661-661f). DFC's subsidy cost estimates take into account, among other things, interest and fees it charges its customers for loans, loan guarantees, and insurance, as well as estimated default costs.
[42] DFC's ODP is responsible for conducting the environmental, social, and economic clearances as well as assessing potential development impact for all DFC investments during the origination phase. Specifically, ODP's Economic and Development Impact Assessment Division determines whether or not a potential investment would negatively impact U.S. jobs and assess the investment's potential development impact.
[43] For loans between $20 and $50 million, credit committee and investment committee review and approval are required. For loans exceeding $50 million as well as any hybrid debt transaction, approval from DFC's Board of Directors is also required.

Graphic 6: Site monitoring will require travel to some DFC-funded investment projects.

Depending on the type of support, project sector, and whether DFC has previously worked with the project counterparty, the origination phase can take anywhere from approximately four months to over a year (see **Appendix III: Timeline of Key Activities for Sampled Investments**). After the first disbursement of financial support, the project moves from the origination phase into the "monitoring phase". DFC monitoring can be broken down into three categories: financial monitoring (i.e., whether the project counterparty is financially sound and able to meet its financial commitment to DFC); monitoring of compliance with E&S covenants; and monitoring of development impact.

DFC's financial monitoring is conducted by various departments depending on the type of financing tool. Financial monitoring for loans and loan guaranties can include activities such as monitoring financial covenants and reporting requirements; managing disbursement requests; performing periodic site visits; drafting periodic loan reviews; working with stakeholders to implement waivers, amendments, or project loan restructurings should they become necessary; recommending write-offs; and processing the close-out of the project.

The financial monitoring of equity and investment funds is conducted by DFC's Office of Equity and Investment Funds and is performed by the same officials that originated the investment project. The financial monitoring of these types of projects can include a quarterly performance measurement report (which addresses the performance of investment fund portfolios as well as any disbursements or capital calls, new commitments, and underlying investment activity), a quarterly fund review report (which is a summary for each fund in their portfolio listing high-level performance metrics), and an annual fund review report (providing a more in-depth analysis of the fund and performance).

While DFC has various divisions that conduct financial monitoring depending on the financing tool, the ODP is responsible for monitoring all DFC projects for E&S compliance and development impact. ODP's Environmental Risk Assessment and Social Risk Assessment Divisions monitor these aspects, while ODP's IMML Division monitors development impact results. Monitoring of E&S compliance and development impact is performed through project self-reporting and information gathered through staff-conducted site visits and third-party contracted site visits and analysis. Performing site visits for most projects is an especially critical monitoring tool for DFC, as it best validates what is actually taking place "on the ground".

DFC's E&S compliance monitoring and development impact monitoring are important factors in ensuring DFC projects comply with E&S requirements and for determining a project's development impact. Project monitoring has been an area where DFC has had prior significant findings. In 2018, DFC's predecessor, OPIC, issued an internal report prepared by the Office of Accountability assessing whether the use of client-reported data, supplemented by selected site visit monitoring, was adequate in achieving program goals.[44] This assessment was conducted in response to a 2015 GAO audit that noted concerns with the agency's monitoring of E&S compliance and its reliance on client-reported data, which can be inaccurate or incomplete.[45] The internal report found that the client-reported data examined was of "dubious quality" but, in the absence of site visits, was the only formal mechanism for which to obtain E&S information from every project financed. Furthermore, it concluded that client-reported data was inadequate to assess E&S compliance as outlined in the agreement terms.

DFC E&S and development impact monitoring help ensure projects comply with requirements.

Both the GAO audit and the Office of Accountability report emphasized the critical importance of project site visit monitoring. While not every project will need a site visit, a structured, risk-based process for managing site visit monitoring will allow DFC officials to meet with counterparties and visit project locations to validate not only what has been reported, but potentially to observe what has not been reported. Based on information gathered during a site visit, DFC officials can work with counterparties to rectify any failures to comply with agreement terms or pursue termination of DFC support. Due to the challenging business environments in which DFC operates, robust monitoring plans and site visit selections need to be in place to ensure project risks are addressed and to ensure DFC fully understands those risks.

For Strategic Level Objectives, Plans, and Measurable Goals for Project Site Visit Monitoring, see recommendations 7-8 in the **Summary of Recommendations and Management Comments**.

Finding #7: Policies and Procedures Lack Site Visit Monitoring Guidance, and Data Is Not Systematically Tracked for Management Analysis and Strategic Plan Monitoring

We reviewed nine DFC policies and procedures that applied to 10 separate monitoring divisions within DFC to assess their guidance on the planning, conducting, and reporting of site visits.[46] Most divisions either do not have or have not finalized adequate site visit monitoring policies and procedures. This would include guidance on the selection and timing of site visits, and information that should be consistently collected when conducting a site visit. Additionally, DFC policies do not require information gathered from site visits to be formally documented and site visit reports are not centrally stored and available for other officials to access. This prevents DFC from tracking site visit data against any established strategic goals for site monitoring. We inquired with ODP regarding the number of site visits that had been performed in the past year and ODP responded that this data is not readily available and would take significant effort to compile. Given the importance of site visit work in comparison to counterparty self-reported data, as well as considering lessons learned and best practices from these site visits for its future investments, DFC

[44] OPIC's Office of Accountability, *Assessment of OPIC's Environmental and Social (E&S) Monitoring of Projects*, February 7, 2018, p. 63.
[45] GAO, *Overseas Private Investment Corporation, Additional Actions Could Improve Monitoring Processes*, GAO-16-64, December 2015, pp. 34-39.
[46] As of June 2023, DFC divisions are organized around investment product. However, the agency is working to organizationally realign divisions by sector within the next fiscal year.

should have more detailed policies and procedures for divisions to reference and share throughout the organization.

For Site Visit Monitoring Guidance, and Data Is Not Systematically Tracked see recommendation 9 in the **Summary of Recommendations and Management Comments**.

Finding #8: Staffing of Office of Development Policy Appears to Be Insufficient to Perform Robust Site Visits in Comparison to Peer Development Finance Institutions

The BUILD Act requires DFC to develop a performance measurement system to evaluate and monitor projects supported by DFC.[47] The performance measurement system must incorporate standards and a method for ensuring appropriate development performance of its portfolio. This includes the measurement of the projected and ex-post-development impact of a project.[48] As reported in our BUILD Act audit, DFC's current performance measurement system to report development impact on a country-by-country basis needs further work to fully comply with these sections of the BUILD Act.[49] DFC has made progress in this area and reported development impact for India in their FY 2022 Annual Report. DFC plans to add additional countries in future years as more data becomes available.

The BUILD Act also requires DFC to include in their annual report analyses of the effects of supported projects, including reviews and analyses of projects' desired development outcomes, and whether or not metrics, goals, and development objectives are being met, including to the extent practical, in the years after the conclusion of projects.[50] DFC's annual report should also provide information on the projections of development outcomes, and whether or not projects are meeting the associated performance measures throughout the life of the project.[51] To address these BUILD Act requirements and enhance development impact measurement and monitoring, DFC established IMML within ODP in August 2021. This was a significant step that DFC took towards monitoring and reporting on development impact.

IMML serves an important purpose as it is responsible for reviewing, analyzing, and managing the development impact of the DFC portfolio on an ongoing basis throughout all phases of an investment, from origination to project close-out, and perhaps beyond. One way in which IMML obtains development impact data is through the submission of development outcome surveys (DOS) from project counterparties.[52] In FY 2022, IMML received and analyzed 52 DOS, and in FY 2023 it expects to receive between 130 to 150 submissions. As previously stated, development impact information is primarily obtained through counterparty self-reporting, and to a lesser extent by DFC staff and third-party contracted site visits and analysis.

In addition to development impact, the BUILD Act requires DFC, as a matter of policy, to use best practices with respect to transparency and environmental and social safeguards and achieve clearly defined economic

[47] The World Bank differentiates monitoring and evaluation by defining monitoring as those information gathering activities that take place when a project is being implemented, whereas evaluation are those activities that take place at the end of a project.
[48] BUILD Act Section 1442(a) and 1442(b)(4)(A).
[49] DFC OIG, *DFC Made Significant Progress Implementing Provisions of the Better Utilization of Investments Leading to Development Act,* DFC-22-005-C, September 22, 2022, p. 10.
[50] BUILD Act Section 1443(b)(1)(A).
[51] BUILD Act Section 1443(b)(3)(A).
[52] Development Outcome Surveys are also known as 008 Forms. These are completed by counterparties and submitted to DFC for review.

and social development outcomes.[53] As previously stated, ODP's Environmental Risk Assessment Division and Social Risk Assessment Division monitor these aspects of a project.

Both the 2015 GAO report on OPIC and the agency's follow-up internal report, completed by the Office of Accountability, commented on the Corporation's limited staffing in comparison to the World Bank Group's IFC. According to IFC officials at the time, site visits were conducted for all projects in its portfolio, then valued at $45.8 billion, on a regular basis. IFC's E&S teams visit all projects once every two years. They also conduct a limited number of post-completion evaluations to assess project impact. In 2017, IFC said it employed 80 full-time environmental and social specialists, together with approximately 20 short-term consultants. Currently, British International Investment (BII) has a staff of 25 focused on impact clearance and management for a total portfolio of $7.1 billion.[54] FinDev Canada, a much smaller development finance institution with a total portfolio valued at $658 million invested in 36 projects, has approximately five staff focused on impact clearance and management.

In comparison, as of June 2023, DFC had 1,266 active projects, with a combined total exposure of $35.4 billion.[55] IMML has a total of 11 full-time staff with four vacancies it plans to fill. The Environmental Risk Assessment Division has a total of 12 full-time staff and eight vacant positions, while the Social Risk Assessment Division has a total of 10 full-time staff and five vacant positions. See the table below for a summary of DFC's ODP staffing. This brings the number of total staff in these divisions to 33 with 17 open vacancies, a significantly smaller number than IFC, BII, and FinDev Canada when compared to the size of the portfolios being managed. While some vacancies have been filled, given the importance of ODP and specifically IMML's role in the mission of DFC, it appears the department is understaffed in comparison to peer development finance institutions. The table below summarizes staffing in the ODP divisions that monitor projects for compliance with environmental and social covenants and development impact.

Table 1: DFC's Office of Development Policy Staffing.[56]

DFC Financial Exposure	ODP Divisions	Fulltime Employees	Vacancies
$35.4 Billion	Impact Management, Monitoring, and Learning	11	4
	Environmental Risk Assessment Division	12	8
	Social Risk Assessment Division	10	5
	Total	**33**	**17**

For Staffing of Office of Development Policy, see recommendation 10 in the **Summary of Recommendations and Management Comments**.

[53] BUILD Act Section 1411(4) and (6).
[54] BII is the United Kingdom's development finance institution and was formally known as Commonwealth Development Corporation Group.
[55] Active commitments refer to the number of unique, non-repeating project numbers in DFC's records system.
[56] ODP Organization Chart, June 2023.

Our Site Visits Did Not Detect Noncompliance with the Xinjiang Supply Chain Business Advisory

Photo 4: Images of a solar plant in Northern India where the team verified if owners were aware of US initiatives to ensure materials used to make solar panels were not purchased from a list of prohibited PRC companies.

The government of the People's Republic of China continues to carry out crimes against humanity and genocide against Uyghurs and other ethnic and religious minority groups in the Xinjiang Uyghur Autonomous Region (Xinjiang) of China. As a result, in July 2021, U.S. Customs and Border Protection banned sourcing labor or goods from Xinjiang, from entities elsewhere in China connected to the use of forced labor individuals from Xinjiang, and from entities outside of China that source inputs from Xinjiang. The Department of Labor added polysilicon, a key raw material for solar panels, as an update to the *List of Goods Produced by Child Labor or Forced Labor* due to evidence of production of polysilicon by forced labor in China. In response to these U.S. government efforts, in August 2021, DFC implemented policies that require intermediaries, through which it provides support, to agree to not use DFC proceeds to purchase solar panels manufactured by entities subject to U.S. government sanctions. DFC policies further prohibit the purchase of solar panels listed or manufactured by entities listed by the Forced Labor Enforcement Task Force, as described under Section 2 of the Uyghur Forced Labor Prevention Act.

It is important to note that these policies came into effect after DFC invested in the solar projects from this audit sample. We noted that DFC monitoring officials were also made aware of this issue when this policy was implemented. During the fieldwork phase of this audit, we determined that officials at the solar plants visited by the audit team were aware of these prohibitions and had policies in place to ensure compliance with DFC policies. We inspected the solar panels during our visit and did not detect any panels from prohibited sources for the solar panels reviewed.

Finding #9: DFC Needs to Improve the Monitoring, Tracking, and Reporting of Significant Environmental and Social Events, Particularly Fatalities and Serious Injuries Related to Environmental or Social Covenants

DFC counterparties are required to report incidents of significant environmental and social events for projects DFC has classified as high risk for significant adverse environmental and/or social impacts.[57] DFC generally defines significant E&S events in its agreements with counterparties as incidents that involve the

[57] DFC categorizes high risk projects as Category A. DFC's ESPP Section 6.4 requires agreements involving Category A projects to include the timely notification to DFC of any significant environmental and/or social event that has occurred.

loss of life or have a material adverse impact on the environment or local communities. Counterparties are required to report these events to DFC within 24 hours after they become aware of such an incident. Furthermore, DFC requires the counterparties of all projects classified as high risk, and some projects categorized as medium risk, to provide an annual social and environmental report that includes information pertaining to accidents impacting people or the environment, including those resulting in a disability or loss of life.[58]

DFC's $54.9 million equity investment in Renewable Energy Project No. 4 was categorized as high risk; therefore, the Fund was required to report all significant E&S events. In April, May, and October 2022, the Fund's officials informed DFC of three significant E&S events, resulting in a total of three fatalities and two serious injuries. DFC's ODP team traveled to India in November 2022 to perform site visits at some of the Fund's various sites. While the DFC team had been informed of the fatalities prior to their visit, they did not visit the locations where the significant E&S events had occurred. RMA and OIG personnel were not made aware of these fatalities prior to our site visit. During the course of our site visit, we inquired and were informed by the Fund's management that three fatalities had occurred on various downstream investments, including one fatality and two serious injuries at a solar field we visited, further described in **Appendix IV: Summary of Significant Environmental and Social Events.**

Although DFC was notified of fatalities and accidents, DFC did not visit the sites where these events occurred during site visits to India.

When we asked DFC officials how significant E&S events impacted the site monitoring plan, DFC officials could only state that it depended on the circumstances surrounding the event, thereby making determinations on a case-by-case basis. For example, ODP officials said they did not visit the locations where fatalities had occurred because they appeared to have been caused by employees not following already established safety protocols and therefore were preventable. DFC was not able to demonstrate that fatalities and serious injuries are incorporated into the planning process for project monitoring. The various DFC departments we contacted could not provide a comprehensive project site monitoring plan, and policies and procedures pertaining to site visit monitoring either did not exist or lacked such information.

We asked DFC officials how significant E&S events occurring at DFC-funded projects are collected and reported. They said when such an event is reported to DFC, the information is provided to the Office of External Affairs to respond to any inquiries received from external parties concerning the incident.[59] However, DFC officials were unable to provide us with a comprehensive list of significant E&S events and stated that to gather this information would be time-consuming because it would require manually reviewing individual project documents. DFC officials said that such information is not centrally maintained because they have not identified it as necessary data to maintain and report. The BUILD Act requires DFC to "use best practices with respect to transparency and environmental and social safeguards" to provide countries a "robust alternative" to state-directed authoritarian governments and U.S. strategic competitors.[60] DFC has not publicly reported these fatalities, or any significant E&S event, in its FY 2020-2022 Annual Reports. While DFC requires the Fund and other counterparties to report significant E&S events, DFC itself does not have a comprehensive, systematic process to track and transparently report such incidents. This lack of reporting does not align with the BUILD Act's policy that DFC uses best practices with respect to transparency, especially since DFC's purpose includes providing a contrast to closed,

[58] DFC categorizes medium risk projects as Category B. DFC's ESPP section 7.7 outlines the annual environmental and social reporting requirements.
[59] The Office of External Affairs is DFC's lead communicator to all external audiences, including Congress, media, and the American public.
[60] BUILD Act Section 1411(6).

authoritarian governments. Further, the BUILD Act[61] requires DFC, in its Annual Report, to report the compliance of projects supported by the Corporation under Title II with human rights, environmental, labor, and social policies, or other such related policies that govern the Corporation's support for projects, promulgated or otherwise administered by the Corporation. We believe this would encompass the reporting of significant environmental and social events related to DFC projects.

The February 7, 2018, Assessment of the OPIC Environmental and Social Monitoring of Projects, conducted by OPIC's Office of Accountability, recommended a site visit be conducted to any location that had a "fatality, notice from a government official, significant community protest, or significant emergency event."[62] At the time the report was issued, OPIC management reported that this had been adopted on September 28, 2017. While this internal recommendation was made under DFC's predecessor OPIC, DFC management should continue to either adhere to this recommendation or have clear, updated monitoring policies and procedures addressing how significant E&S events are monitored.

DFC's lack of a central reporting system concerning significant E&S events makes it challenging for officials across the agency to properly monitor projects, particularly projects it has identified as high risk for significant adverse environmental and/or social impacts. It demonstrates that, while DFC has policies, procedures, and databases in place for projects during the origination phase, such mechanisms need to be improved for use during the critical E&S monitoring and reporting phase of a project. Moreover, collecting data on significant E&S events in a central location makes information-sharing within DFC easier and less reliant on the institutional memory of experienced employees who depart from DFC. This information can also be used to determine any patterns (e.g., countries, projects, sectors) regarding serious injuries or fatalities, which could inform DFC personnel regarding needed changes to policies, future agreements, or particular E&S covenants that are needed or that should be adjusted.

For significant environmental and social events, see recommendations 11-13 in the **Summary of Recommendations and Management Comments**.

[61] BUILD Act Section 1443(a)(4).
[62] OPIC's Office of Accountability, *Assessment of OPIC's Environmental and Social (E&S) Monitoring of Projects*, February 7, 2018, p. 5.

Conclusion

Photo 5: A view of a solar panel field in Northern India.

Our audit determined DFC supported local country development in alignment with its mission and BUILD Act requirements regarding project counterparty considerations. However, we determined DFC did not adequately support a waiver of ESPP, resulting in $54.91 million in unsupported questioned costs. We also determined that DFC should develop stronger policy around the use of subordinated debt, improve its governance of site visit monitoring, and implement better monitoring, tracking, and reporting of significant environmental and social events, including fatalities and serious injuries. Based on our review we determined:

DFC Did Not Adequately Support a Waiver of Environmental and Social Policy Standards on a Project, Which Resulted in $54.91 Million in Unsupported Questioned Costs: DFC's justification for approving the blanket waiver of ESPP policies pertaining to IFC Performance Standards for the investment in Renewable Energy Project No. 4 was that the investment was highly developmental and aligned with U.S. foreign policy interests. This justification can be stated for the majority of DFC projects and does not explain why this particular project was unique and thus justified a waiver. By waiving IFC Performance Standards, DFC undermined its BUILD Act mandate to adhere to best practices concerning environmental and social safeguards.

DFC Has Not Developed Sufficient Internal Controls to Support the Approval Process for Projects Financed Through Subordinated Debt: DFC has not developed a policy for originating subordinated debt financing. Additionally, DFC can use the OCRO to help identify and manage risk associated with subordinated debt at the enterprise level. Completing and implementing this policy prior to initiating new projects that use subordinated debt will help to strengthen the process for assessing proposed subordinated debt financing.

DFC's Records Management System Can Be Unreliable in Compiling a Complete Set of Documents for Individual Projects: DFC's official records management system, Content Manager, can be unreliable in compiling a complete set of required documents for projects. The audit team found that Content Manager has issues interfacing with other records management databases such as Insight, and certain required documents were missing in Content Manager for all 17 projects.

DFC Does Not Have Strategic Level Objectives, Plans, and Measurable Goals for Project Site Visit Monitoring: DFC has various divisions that conduct monitoring depending on project type. However, DFC does not have strategic level objectives, plans, and measurable goals for project site visit monitoring. Further, there is no formal process for DFC divisions to develop a yearly site visit monitoring plan that would be linked to strategic plans and goals. Moreover, DFC's current site visit monitoring process at the division level is ad hoc, informal, and not driven by strategic goals. Further, policies and procedures lack site visit monitoring guidance, and data is not tracked for management analysis and strategic plan monitoring. Additionally, staffing of the ODP appears to be insufficient to perform robust site visits.

Policies and Procedures Lack Site Visit Monitoring Guidance, and Data Is Not Systematically Tracked for Management Analysis and Strategic Plan Monitoring: Most of the monitoring divisions within DFC lack finalized adequate site visit monitoring procedures. DFC does not have formal procedures for gathering and storing documentation from site visits which inhibits any enterprise level tracking against strategic goals. Additionally, ODP was unable to readily provide information regarding the number of site visits performed in the last year.

Staffing of ODP Appears to Be Insufficient to Perform Robust Site Visits in Comparison to Peer Development Finance Institutions: Per BUILD Act requirements, DFC must develop and improve its monitoring and reporting systems to ensure appropriate development of its portfolio. IMML was established within ODP as a step towards improving these systems and is responsible for reviewing, analyzing, and managing the development impact of the DFC portfolio on an ongoing basis. The number of counterparties self-reporting information in the DOS, which IMML primarily relies on for development impact information, is expected to almost triple in FY 2023.

According to reports from a 2015 GAO report and an internal report from the Office of Accountability, IFC's E&S teams visited all projects in the $45.8 billion portfolio at least every two years. Additionally, IFC, in 2017 employed 80 full-time environmental and social specialists with approximately 20 short-term consultants. DFC, with a $35.4 billion portfolio, had 11 full-time staff in IMML with four additional vacancies as of June 2023. When compared to IFC, along with BII and FinDev Canada, IMML's staffing is significantly smaller when accounting for the size of the respective portfolios.

DFC Needs to Improve the Monitoring, Tracking, and Reporting of Significant Environmental and Social Events, Particularly Fatalities and Serious Injuries: For projects DFC has classified as high risk for significant adverse environmental and/or social impacts, DFC requires counterparties to report incidents of significant environmental and social events. DFC officials were unable to provide a comprehensive list of significant E&S events reported to them and stated that gathering such information would be time-consuming because it would require manually reviewing individual project documents. DFC officials stated that such information is not centrally maintained because they have not identified it as necessary data to maintain and report. DFC's lack of a central reporting system or clear monitoring policies and procedures concerning significant E&S events makes it challenging for officials across the agency to properly monitor projects, particularly projects it has identified as high risk for significant adverse environmental and/or social impacts.

We made 13 recommendations to improve DFC's strategic approach to advancing its mission and to strengthen its internal control system. See **Summary of Recommendations and Management Comments** for additional details.

Summary of Recommendations and Management Comments

Recommendations for the Waiver of Environmental and Social Covenants (Finding 3):

Recommendation No. 1: Revise Directive OD-004 to include the Office of the Chief Risk Officer review of waivers of the DFC Environmental and Social Policy and ensure coordination with the Office of Accountability.

> **Management Response:** DFC concurs with this recommendation and will revise this Directive accordingly. DFC notes that it issued internal management guidance concerning any future ESPP waivers in October 2021. That same guidance was subsequently incorporated into ODP's Office Directive in November 2022.
>
> **Responsible Party:** Office of General Counsel
>
> **Target Resolution Date:** 1st Quarter of FY 2024

Recommendation No. 2: Include any waivers of DFC Environmental and Social Covenants as part of the Congressional Notification process.

> **Management Response:** DFC concurs with this recommendation and updated its policies and procedures for the Congressional Notification process in the 3rd quarter of FY 2023.
>
> **Responsible Party:** Office of External Affairs
>
> **Target Resolution Date:** Not applicable - Completed upon report issuance.

Recommendations for DFC's Use of Subordinated Loans (Finding 4):

Recommendation No. 3: Ensure DFC develops a policy regarding the use of subordinated debt, to include the appropriate uses and approval of subordinated debt.

> **Management Response:** DFC concurs with this recommendation. DFC will revise its Loan and Guaranty Directive to clarify that the Corporation's existing processes around the origination and risk management of subordinated debt are sufficient.
>
> **Responsible Party:** Office of General Counsel
>
> **Target Resolution Date:** 1st Quarter of FY 2024

Recommendation No. 4: Explicitly incorporate DFC's subordinated debt usage into the Corporation's ERM process.

> **Management Response:** DFC concurs with this recommendation and will update its Office of the Chief Risk Officer Directive accordingly.

Responsible Party: Office of the Chief Risk Officer

Target Resolution Date: 1st Quarter of FY 2024.

Recommendations for Records Management (Finding 5):

Recommendation No. 5: Until Content Manager and Insight systems interface properly; develop and implement improved internal controls that verify applicable documents are uploaded in Insight and that appropriate workflows are followed.

Management Response: DFC concurs with this recommendation and will continue to reduce the filing backlog while simultaneously addressing the root causes of the system interface issues.

Responsible Party: Office of Information Technology

Target Resolution Date: 1st Quarter of FY 2024

Recommendation No. 6: Ensure the interface between Insight and Content Manager systems is functional so that applicable project documents are readily available and properly stored.

Management Response: DFC concurs with this recommendation. DFC has acquired new software to fix these interface issues and is actively testing the software deployment.

Responsible Party: Office of Information Technology

Target Resolution Date: 1st Quarter of FY 2024

Recommendations for Strategic Level Objectives, Plans, and Measurable Goals for Project Site Visit Monitoring (Finding 6):

Recommendation No. 7: Direct DFC's CDO and CRO, in coordination with the Office of Accountability, to advise ODP and the OFPM on strategic goals for annual site visit monitoring. This should include a process for publicly reporting plans, goals, and actual performance.

Management Response: DFC concurs with this recommendation. The Office of Development Policy and the Office of Financial and Portfolio Management will update their respective policies and procedures to formalize the process of setting annual goals for site visit monitoring. Policies and procedures will also be amended to include an advisory consultation on each office's annual plans by the Chief Development Officer, Chief Risk Officer, and Office of Accountability. In addition, DFC will determine appropriate public reporting of site visit data and report accordingly on a periodic basis.

Responsible Party: Office of Development Policy; Office of Financial and Portfolio Management; Office of the Chief Development Officer; Office of the Chief Risk Officer; Office of External Affairs.

Target Resolution Date: 3rd Quarter of FY 2024

Recommendation No. 8: Ensure all divisions update and finalize site visit monitoring policies and procedures to align with the agency's strategic goals.

> **Management Response:** DFC concurs with this recommendation. DFC offices with a project monitoring role will update their respective site visit policies and procedures for alignment with strategic goals established for site visit monitoring.
>
> **Responsible Party:** Office of Development Policy; Office of Financial and Portfolio Management; Office of Equity and Investment Funds; Office of Development Credit, Mission Transaction Unit; Office of Structured Finance and Insurance; Office of the Chief Development Officer; Office of the Chief Risk Officer; Office of External Affairs.
>
> **Target Resolution Date:** 3rd Quarter of FY 2024

Recommendations for Site Visit Monitoring Guidance, and Data Is Not Systematically Tracked (Finding 7):

Recommendation No. 9: Develop a system to centrally track site visit reporting results that is accessible to staff for cross-monitoring purposes. The system should facilitate the formal sharing of lessons learned and trends identified during site visits for all phases of DFC's investment decision-making.

> **Management Response:** DFC concurs with this recommendation and will develop and implement policy, procedure, and system changes to facilitate this recording and sharing of information.
>
> **Responsible Party:** Office of Information Technology.
>
> **Target Resolution Date:** 3rd Quarter of FY 2024

Recommendations for Staffing of Office of Development Policy (Finding 8):

Recommendation No. 10: Conduct an internal workforce assessment of ODP to determine the appropriate current and future staffing needs and budget resources to perform site visit monitoring to assess E&S compliance and development impact.

> **Management Response:** DFC concurs with this recommendation and will complete an analysis of current and future staffing needs within the Office of Development Policy.
>
> **Responsible Party:** Office of Development Policy.
>
> **Target Resolution Date:** 2nd Quarter of FY 2024

Recommendations for Significant Environmental and Social Events (Finding 9):

Recommendation No. 11: Develop a system to track all significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments.

Management Response: DFC concurs with this recommendation and will develop and implement a system to track these events.

Responsible Party: Office of Development Policy; Office of Information Technology

Target Resolution Date: 2nd Quarter of FY 2024

Recommendation No. 12: Report significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments to DFC's Board of Directors and report such incidents in the Annual Report.

Management Response: DFC concurs with this recommendation and with the OIG's reporting that none of the mentioned environmental and social events were related to a lack of adherence to DFC's contractual commitments. However, to improve reporting and transparency, DFC will institute processes to report such data to the Board of Directors and in the Annual Report.

Responsible Party: Office of Development Policy; Office of External Affairs

Target Resolution Date: 1st Quarter of FY 2024

Recommendation No. 13: Revise relevant policies and procedures to better define how significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments impact DFC's monitoring site visit priorities, annual plans, and/or schedule.

Management Response: DFC concurs with this recommendation and will articulate in policies and procedures how these events impact the agency's approach to site visit monitoring.

Responsible Party: Office of Development Policy

Target Resolution Date: 1st Quarter of FY 2024

Evaluation of Management Comments

We received initial management comments on the draft report from DFC on October 19, 2023, in which they concurred with all 13 recommendations. However, their response did not include their agreement or disagreement with the report's $54.91 million monetary impact. DFC provided its revised management comments disagreeing with the report's monetary impact on November 2, 2023 (see **Appendix V** for DFC's comments in their entirety).

Concerning the monetary impact, we stand by the evidence presented in the report subsection titled **$54.91 Million of DFC's Investment in Renewable Energy Project No. 4 Is Deemed Unsupported Questioned Costs** (see report pages 9-14 of 49). While OIG agrees that DFC had adequate documentation supporting the approval of the investment, DFC did not have adequate documentation to justify the blanket waiver of IFC Performance Standards on Social and Environmental Sustainability. Furthermore, we consider DFC's full commitment of $54.91 million as unsupported questioned costs as this is the total amount DFC will be expending on the project.

DFC concurred with our findings and all 13 of our recommendations and agreed to complete final action on the recommendations by June 30, 2024. After reviewing DFC's response, we consider them to be responsive to our recommendations. Further, Recommendation 2 will be closed upon issuance of our report. The remaining 12 recommendations are open until DFC provides documentation to verify appropriate actions have been taken.

Appendix I: Objectives, Scope, and Methodology

This was a follow-up audit of the USAID OIG audit of the OPIC Chile Energy Sector Portfolio completed in 2019 (9-OPC-19-002-P). Per DFC OIG consultations with Congress, the objectives of this audit were the same, as follows:

- determine if DFC involved the U.S. private sector and supported local country development in alignment with its mission;
- assess the inputs, data, and analyses used to assess and approve the projects; and
- assess the process and internal controls DFC used to identify and mitigate certain risks.

RMA conducted this audit in accordance with the Yellow Book issued by the Comptroller General of the United States. Those standards required us to plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Additional guidance used include:

- Federal Credit Reform Act of 1990
- GAO (Green Book), *Standards for Internal Control in the Federal Government*
- GAO, "Overseas Private Investment Corporation: Additional Actions Could Improve Monitoring Processes" GAO-16-24
- Office of Accountability Review: Assessment of OPIC's E&S Monitoring Projects, February 7, 2018

The scope of the audit was the assessment of the integration and efficiency of DFC's policies, procedures, and processes regarding investments in renewable energy and financing of MSMEs in India. This audit served as a follow-up to the issues identified in USAID OIG's audit report: OPIC Investments Increased Chile's Energy Capacity, but Weak Processes and Internal Controls Diminish OPIC's Ability to Gauge Project Effects and Risks (Audit Report 9-OPC-19-002-P). This audit assessed projects in India (versus Chile) and covered the renewable energy and finance sectors.

We conducted the audit from June 2022 through July 2023. India was selected because it has the largest DFC project portfolio out of any single country. Using the entire universe of DFC's Indian energy and MSME financing projects, the audit team selected a sample of 17 projects: eight renewable energy projects and nine financing projects. 15 of the sample projects were initiated by DFC and two were initiated by OPIC. The project locations were mapped by state to add proximity as a judgmental factor for site visits. We selected states with diverse projects between MSME and renewable energy projects and applied Probability Proportional to Size methodology to select specific sample sites when more than five sample sites were in the selection pool. The remaining two projects were selected from the legacy scope of one MSME and one renewable energy OPIC projects. From this universe, OIG and RMA selected the two highest valued projects within scope between FY 2016-2017. The total committed amount for the 17 selected projects was approximately $1.2 billion.

The sample selections were used as case studies to assess how DFC met the audit objectives. We also reviewed monitoring compliance per metrics defined by ODP under the BUILD Act. Additionally, the audit assessed DFC's financial program policies and procedures, environmental and social policies and procedures, clearance documents, and loan agreements.

Our tests and reviews included performing entity-level, program, and internal control reviews and walkthroughs, including DFC's source systems and documentation. We also tested criteria associated with the origination and monitoring of the projects and reviewed and assessed DFC project plans and status reports.

For three weeks in February and March 2023, RMA and DFC OIG visited India to conduct site visits to eight sample projects: four renewable energy projects and four MSME financing projects. For the renewable energy projects, the trips included visits to fund recipients' corporate offices throughout India and solar power plants operated by each of the companies. The financial project visits included meetings at the financial intermediaries' offices in India, and meetings with the financial intermediaries' customers at a branch office or the customers' place of business. In total, the audit team interviewed over 100 individuals throughout five Indian states on the trip, and visited offices located in Bengaluru, Gurugram, Jaipur, and Mumbai, as well as solar sites in the states of Rajasthan and Gujarat. We conducted interviews with project employees, contractors, customers, and members of the local community.

Finally, numerous DFC management and staff from various DFC offices were interviewed, including the Office of Development Policy, Office of Development Credit, Office of Financial and Portfolio Management, Office of General Counsel, Office of Administration, Office of Equity and Investment Funds, and Office of External Affairs. We obtained and reviewed internal documents, including directives, policies and procedures, clearance reports, Board reports, flow charts of project approval processes, and records management documentation. We also requested and received documents and data from the various counterparties in India before and after our visits to obtain information about solar panel component sourcing, fatality reporting, customer complaints, and more. Additional information was obtained from publicly available sources. This review included documentation from the period before OPIC became DFC.

Appendix II: Summary of Sampled Investments

This table provides a list of all 17 sampled projects selected for this audit. The purpose of this table is to provide a general overview of the project descriptions, DFC's anticipated development impact, committed amount, and transaction type. There are seven renewable energy projects and eight financial intermediary projects funded by DFC, as well as two OPIC-funded projects (one renewable energy and one financial intermediary).

Table 2: Project Summaries

Project Name	Project Description and DFC Anticipated Development Impact	Committed Amount and Transaction Type
Renewable Energy Project No. 1	Financing the construction and operation of a 100 MW photovoltaic solar power plant in Jodhpur, Rajasthan, India. This project is expected to have a positive developmental impact on India by spurring economic growth in Rajasthan, while providing cheap renewable energy to meet current and growing Indian demand for power.	$50,000,000 Direct Loan
Renewable Energy Project No. 2	Developing, constructing, operating a 300 MW photovoltaic solar power plant in Rajasthan, India. This project is expected to have a positive developmental impact on India by spurring economic growth in Rajasthan, a relatively underdeveloped state in India, while providing inexpensive renewable energy to meet current and growing Indian demand for power.	$142,000,000 Direct Loan
Renewable Energy Project No. 3	Mitigating the potential for near term decline in cash flows due to declining credit profiles of Indian banks. This project is expected to have a highly developmental impact on India by supporting the continued development and operations of the company's extensive renewable power portfolio.	$75,000,000 MFF II Liquidity (Direct) Loan
Renewable Energy Project No. 4	Investing in infrastructure in India including transportation, energy, and utilities. The fund is expected to have a positive developmental impact in India by making investments in infrastructure projects which will have outsized impacts for the overall population of India.	$54,910,000 Equity Investment
Renewable Energy Project No. 5	Financing the construction and operation of a 50 MW photovoltaic solar power plant in Amreli, Gujarat, India. This project is expected to have a positive developmental impact on India by spurring economic growth in Gujarat, and providing relatively lower cost renewable energy to meet current and growing Indian demand.	$27,300,000 Direct Loan
Financial Intermediary Project No. 1	Expanding MSMEs and individuals in India for the purchase of new and used vehicles for commercial use. The project is expected to have a highly developmental impact on India through the expansion of the project company's rural MSME portfolio.	$14,625,000 Investment Guaranty

Project Name	Project Description and DFC Anticipated Development Impact	Committed Amount and Transaction Type
Financial Intermediary Project No. 2	Financing the expansion of the company's portfolio of loans to MSMEs in India for the purchase of new and used vehicles. The project is expected to have a highly development impact in India through support for the company's expansion of credit for commercial vehicle purchases by MSMEs, often owner operators.	$250,000,000 Direct Loan
Financial Intermediary Project No. 3	Providing a Tier 2 subordinated unsecured loan to support the bank's operations during the economic downturn caused by the COVID-19 pandemic. This project is expected to have highly developmental impact in India through the support of a financial institution during a difficult economic period.	$100,000,000 Direct Loan
Financial Intermediary Project No. 4	Financing the expansion of the company's small and medium-sized enterprise (SME) portfolio in India. This transaction is expected to have a highly developmental impact to support lending to SMEs in India, with half of the loans under the guaranty supporting women-owned or operated SMEs.	$50,000,000 Loan Guaranty
Financial Intermediary Project No. 5	Investing in a diversified portfolio of high impact, growth-stage companies in the financial inclusion and healthcare sector in India. The fund is expected to have a positive developmental impact in India by making private equity investments in growing firms that utilize technology to offer either innovative products related to healthcare or loans for MSMEs.	$15,000,000 Investment Guaranty
Renewable Energy Project No. 6	Financing the construction and operation of a 105 MW photovoltaic solar power plant in Gujarat, India. This project is expected to have a highly developmental impact on India by providing inexpensive renewable energy to meet current and growing Indian demand for power.	$53,500,000 Direct Loan
Renewable Energy Project No. 7	Making minority and majority growth equity investments in Indian companies. This fund is expected to have a highly developmental impact in India by supporting companies that provide solutions to promote resource efficiency and sustainability focused on energy efficiency, clean energy value chain, water, and environmental products and services.	$30,000,000 Equity Investment
Financial Intermediary Project No. 6	Providing debt financing to impact-driven SMEs in financial inclusion, affordable housing, healthcare and more. The project will have a highly developmental impact on the Indian economy through the provisions of loans to impact oriented financial institutions and SMEs.	$20,000,000 Direct Loan

Project Name	Project Description and DFC Anticipated Development Impact	Committed Amount and Transaction Type
Financial Intermediary Project No. 7	Providing mostly debt capital to non-banking finance companies and microfinance institutions as well as companies that meet the 2X Challenge criteria. This project is expected to have a highly developmental impact by expanding the availability of MSME lending in India across different sectors including agriculture, commercial vehicles, housing and consumer loans.	$50,000,000 Direct Loan
Financial Intermediary Project No. 8	Financing the expansion of the financial intermediary's microfinance portfolio. This project is expected to have a highly developmental impact by expanding the availability of microfinance lending to women in India. This lending will help to close the $567 million finance gap facing Indian women entrepreneurs.	$14,625,000 Investment Guaranty
Renewable Energy Project No. 8	Developing a 100 MW photovoltaic solar power project located in Telangana, India. The project is expected to have a highly developmental impact as it will generate renewable energy for India.	$74,020,695 OPIC Investment Guaranty
Financial Intermediary Project No. 9	Supporting the strategic growth of the bank's loan portfolio for MSMEs. This project is expected to have a highly developmental impact by expanding the availability of credit to MSMEs in India.	$225,000,000 OPIC Investment Guaranty
Total Committed Amount		**$1,245,980,695**

Appendix III: Timeline of Key Activities for Sampled Investments

The table below presents the four important milestone dates indicating significant stages within a project lifecycle for all 17 sampled projects.

Table 2: Project Milestones

Project Name	Start Date of Origination Process[63]	Commitment Date	Final Agreement Date[64]	First Disbursement Date
Renewable Energy Project No. 1	4/26/2019	5/12/2020	1/15/2021	2/11/2021
Renewable Energy Project No. 2	6/26/2018	5/27/2020	5/27/2020	8/11/2021
Renewable Energy Project No. 3	7/5/2018	9/16/2020	2/23/2021	3/31/2021
Renewable Energy Project No. 4	5/11/2020	12/16/2020	12/16/2020	1/5/2021
Renewable Energy Project No. 5	4/26/2019	5/22/2020	4/2/2021	5/5/2021
Financial Intermediary Project No. 1	3/20/2020	9/24/2021	12/7/2021	1/31/2020
Financial Intermediary Project No. 2	7/29/2021	12/17/2021	5/17/2022	6/1/2022
Financial Intermediary Project No. 3	4/6/2020	12/20/2021	4/29/2022	5/13/2022
Financial Intermediary Project No. 4	8/5/2020	8/31/2021	8/31/2021	3/31/2022
Financial Intermediary Project No. 5	4/29/2019	10/13/2020	5/3/2021	5/17/2021
Renewable Energy Project No. 6	7/5/2018	6/19/2020	2/12/2021	3/25/2021
Renewable Energy Project No. 7	1/27/2020	9/28/2020	12/22/2020	3/16/2021
Financial Intermediary Project No. 6	6/14/2019	3/3/2020	3/11/2020	4/23/2020

[63] The start of the origination process depends on a variety of factors such as the counterparty's initial application submission date, DFC's past relationship, if any, with the counterparty, and how the origination team decides to proceed with a certain project. Therefore, we selected the earliest date found among the following documents: 1) Project Screening Approval Dates, 2) Retainer Letter Dates, and 3) Initial Application Submission Date.
[64] This date encompasses any final agreed-upon contracts (Finance Agreement, Loan and Guaranty Agreement, Side Letter, Contribution Letter, Note Purchase Agreement, etc.) between DFC (or OPIC) and the counterparty.

Project Name	Start Date of Origination Process[63]	Commitment Date	Final Agreement Date[64]	First Disbursement Date
Financial Intermediary Project No. 7	9/26/2019	5/8/2020	12/1/2020	12/18/2020
Financial Intermediary Project No. 8	3/27/2020	8/31/2020	12/10/2020	4/29/2021
Renewable Energy Project No. 8	7/17/2015	9/23/2016	4/3/2017	8/2/2017
Financial Intermediary Project No. 9	7/1/2016	9/28/2016	6/1/2017	7/26/2017

Appendix IV: Summary of Significant Environmental and Social Events

The table below summarizes the three significant Environmental and Social events that occurred on three separate project sites that are associated with DFC's investment in Renewable Energy Project No.4.

Table 3: Summary of Significant Environmental and Social Events

Site Description and Location	Summary of Event	Fatality & Injury Total
300 MW Solar Power Plant – Rajasthan	On May 4, 2022, a workman employed by a subcontracted firm was found unresponsive below a solar panel. He was there assisting in the inspection of the plant's solar panel mounting system stability and alignment and to collect any leftover materials for disposal. He was immediately taken to the nearest hospital, where upon arrival he was declared deceased (later determined by electrocution).	One Fatality
250 MW Solar Power Plant – Rajasthan	On April 19, 2022, three technicians employed by the power plant sustained severe burn injuries due to a rod mistakenly connected to two live (not isolated) busbars. The technicians were performing preventative maintenance activities. All three were taken to a nearby hospital and subsequently transferred to other medical centers to assist in recovery. Individual A succumbed to his injuries on April 26, 2022, after suffering burns on 98 percent of his body. Individual B was discharged on April 22, and Individual C was discharged on May 18, 2022, both in stable condition.	One Fatality and Two Severe Injuries
Private Freight Terminal – Gujarat	On October 7, 2022, an external truck driver was walking through the warehouse lot to pick up a recently loaded semi-truck and was fatally struck by a reversing Reach Stacker (a vehicle that loads shipping containers onto semi-truck beds).	One Fatality

Appendix V: Management Comments

DFC U.S. International Development Finance Corporation

MEMORANDUM October 19, 2023

TO: Anthony Zakel
Inspector General
DFC – Office of the Inspector General

FROM: Scott Nathan
Chief Executive Officer

SUBJECT: DFC's Management Comments to "DFC Can Improve Oversight of Renewable Energy and Financing Projects in India"

The U.S. International Development Finance Corporation (DFC) response to the recommendations made by the DFC Office of Inspector General (OIG) in the report titled *DFC Can Improve Oversight of Renewable Energy and Financing Projects in India* is provided below.

DFC plays a vital role in sustaining the US government's commitment to advancing private sector investments in India and deepening the economic ties between both countries. Reflecting this commitment, as of 6/30/23, DFC has invested $3.16 billion across over 140 transactions, representing 9% of DFC's outstanding portfolio and the agency's largest country exposure. The recommendations from the OIG are timely with DFC seeking to accelerate economic growth and development in India in alignment with U.S. developmental and foreign policy priorities. Insights gained from the OIG can help strengthen the agency's ability to provide access to capital and drive sustainable and measurable impact, both in India and across all the countries in which DFC provides its support.

With respect to the OIG's determination of unsupported questioned costs related to one individual transaction, DFC management is not in concurrence with this position for the following reasons:

1. **The Documentation Was Adequate for the CEO and Board of Director's Approval of the Cost.**

The Inspector General Act of 1974 ("IG Act") defines unsupported questioned costs as "a finding that, at the time of the audit, the cost is not supported by adequate documentation."[1] DFC contends that the costs in this cited transaction were supported by adequate documentation at the time of the audit.

[1] 5 U.S.C. § 405 (a)(7); 5 U.S.C. § 405 (a)(4)(b)

At time of the audit, which began in June 2022, the OIG reviewed the following documents specifically related to the transaction: the Board Paper, Decision Action Memo, Congressional Notification, and related correspondence with Congress. In addition, the OIG reviewed the agency's Environmental and Social Policy and Procedures ("ESPP") and the revised Office of Development Policy Directive.

The report stated, "The rationale provided by DFC for the waiver of ESPP – that the project was a highly developmental project aligned with foreign security goals – could be stated for many projects that DFC supports and is not unique to the Fund." That this project was "highly developmental" and "aligned with foreign security goals" is accurate and seemingly not in dispute by the OIG. The rationale and basis for DFC's support of this transaction is, however, more than this one quoted sentence and more than the ESPP waiver.

When the record of project documentation in viewed in its totality – a body of information that was presented to and thoroughly reviewed by the Board of Directors and CEO – the support for this cost by DFC's decision makers becomes evident. The documented facts and circumstances surrounding this transaction were presented to DFC's Board of Directors and the CEO, and the OIG's reporting did not identify any gaps in the presentation of information, indicators that the Board of Directors and CEO were not given adequate information upon which to base their decision to approve the transaction, or evidence that the decision made was unreasonable or inappropriate based on that available information.

Moreover, the materials presented to the Board were supported by extensive documentation and procedures including due diligence by highly experienced DFC staff. In addition, prior to incurring the costs, DFC prepared and approved sophisticated financing documents, as well as disbursement documentation for each incurrence of costs, that also supported the costs to be incurred. The OIG's narrow focus on the waiver justification neglects to consider fully the large body of documentation supporting the costs and the determination by the Board and CEO that adequate documentation was available to make their decision.

Adequacy of information must be assessed in the context of the entire record and what is needed for the Corporation's decision makers. The Board of Directors and CEO found the information presented to be adequate to make a sound decision, and in the absence of clear evidence that such a decision was inappropriate or unreasonable given the totality of the facts and circumstances surrounding the transaction, it is DFC's position that the documentation to approve this transaction and incur the cost was adequate – particularly at the time of the audit - in accordance with the IG Act.

2. **The Procedures Used for the ESPP Waiver Provided Requisite Information to DFC's Decision Makers.**

The OIG seems to imply that DFC was required to have a written process and procedure for ESPP waivers. "Regardless of specific provisions in statutes and regulations, the Supreme Court has said that 'an agency's authority to proceed in a complex area [of] regulation by means of rules of general application entails a concomitant authority to

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provide exemption procedures in order to allow for special circumstances.'"[2] Recognizing that DFC possesses this authority, ESPP waivers were and are extraordinarily rare. Such waivers as identified in this transaction have only been exercised twice in the past forty years, and in the rare instances when one is contemplated, the consideration is treated as the exceptional matter that it represents. The OIG's position that policy guidance was inadequate would need to be supported by specific identifications of material omissions in the information presented to the Board or the CEO which adversely impacted the CEO or Board's decision-making process and might have been reasonably prevented had further policy guidance been available; this report does not identify such a deficiency.

This extreme infrequency of such actions supports DFC's historical position that current project approval documents and project-specific waiver memoranda were sufficient to handle this need for the specific cited project discussed in the report. The fact that, upon subsequent discussions with stakeholders, a written process and criteria were developed by DFC does not alter whether the documentation, and the underlying process to generate it, was adequate at the time of the initial decision.

3. **The BUILD Act Must be Read in its Entire Context.**

The OIG has conflated the statutory requirement to use best practices concerning environmental and social safeguards, which cannot be waived, with DFC's ESPP that adopts the International Financial Corporation (IFC) performance standards and can be tailored and applied at the project level. While DFC cannot waive a statutory requirement, the DFC can forego requiring strict adherence to IFC performance standards to fulfill the many aspects of the BUILD Act. DFC believes the argument made by the OIG puts forth a theoretical concern that the DFC undermined a particular BUILD Act mandate without providing facts that support this concern.

4. **Although Management Does Not Concur with the OIG's Determination of Unsupported Questioned Costs, the OIG Presented an Overstated Calculation.**

DFC does not agree with the OIG using the transaction's commitment value instead of disbursements made at the time of the audit to represent the unsupported questioned costs for DFC financial support products. Audits are conducted as of point-in-time, and at the time of the audit, the amount disbursed for this transaction was roughly 40% of the total commitment, but instead of recording the amount disbursed to-date as the unsupported questioned cost, the OIG elected to project into the future and question disbursements that not only have not been made but will only be made contingent on the project counterparties meeting certain legal covenants and conditions. DFC believes it is inappropriate to question future undisbursed support in this calculation and that the calculation is substantially overstated as of the date of the audit report.

[2] "An Important Member of the Family: The Role of Regulatory Exemptions in Administrative Procedures." P. 298 https://www.administrativelawreview.org/wp-content/uploads/2014/04/An-Important-Member-of-the-Family-The-Role-of-Regulatory-Exemptions-in-Administrative-Procedure.pdf

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The OIG provided DFC with 13 recommendations and DFC's response to each of those recommendations is provided below:

OIG Recommendation No. 1: Revise Directive OD-004 to include the Office of the Chief Risk Officer review of waivers of the DFC Environmental and Social Policy and ensure coordination with the Office of Accountability.

> **Management Response**: DFC concurs with this recommendation and will revise this Directive accordingly. DFC notes that it issued internal management guidance concerning any future ESPP waivers in October 2021. That same guidance was subsequently incorporated into ODP's Office Directive in November 2022.
>
> **Responsible Party**: Office of General Counsel
>
> **Target Resolution Date**: 1st Quarter of FY 2024

OIG Recommendation No. 2: Include any waivers of DFC Environmental and Social Covenants as part of the Congressional Notification process.

> **Management Response**: DFC concurs with this recommendation and updated its policies and procedures for the Congressional Notification process in the 3rd quarter of FY 2023.
>
> **Responsible Party**: Office of External Affairs
>
> **Target Resolution Date**: N/A - Completed

OIG Recommendation No. 3: Ensure DFC develops a policy regarding the use of subordinated debt, to include the appropriate uses and approval of subordinated debt.

> **Management Response**: DFC concurs with this recommendation. DFC will revise its Loan and Guaranty Directive to clarify that the Corporation's existing processes around the origination and risk management of subordinated debt are sufficient.
>
> **Responsible Party**: Office of General Counsel
>
> **Target Resolution Date**: 1st Quarter of FY 2024

OIG Recommendation No. 4: Explicitly incorporate DFC's subordinated debt usage into the Corporation's Enterprise Risk Management process.

> **Management Response**: DFC concurs with this recommendation and will update its Office of the Chief Risk Officer Directive accordingly.
>
> **Responsible Party**: Office of the Chief Risk Officer

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Target Resolution Date: 1st Quarter of FY 2024

OIG Recommendation No. 5: Until Content Manager and Insight systems interface properly, develop and implement improved internal controls that verify applicable project documents are uploaded in Insight and that appropriate workflows are followed.

Management Response: DFC concurs with this recommendation and will continue to reduce the filing backlog while simultaneously addressing the root causes of the system interface issues.

Responsible Party: Office of Information Technology

Target Resolution Date: 1st Quarter of FY 2024

OIG Recommendation No. 6: Ensure the interface between Insight and Content Manager systems is functional so that applicable project documents are readily available and properly stored.

Management Response: DFC concurs with this recommendation. DFC has acquired new software to fix these interface issues and is actively testing the software deployment.

Responsible Party: Office of Information Technology

Target Resolution Date: 1st Quarter of FY 2024

OIG Recommendation No. 7: Direct DFC's Chief Development Officer and Chief Risk Officer, in coordination with the Office of Accountability, to advise the Office of Development Policy and the Office of Financial and Portfolio Management on strategic goals for annual site visit monitoring. This should include a process for publicly reporting plans, goals, and actual performance.

Management Response: DFC concurs with this recommendation. The Office of Development Policy and the Office of Financial and Portfolio Management will update their respective policies and procedures to formalize the process of setting annual goals for site visit monitoring. Policies and procedures will also be amended to include an advisory consultation on each office's annual plans by the Chief Development Officer, Chief Risk Officer, and Office of Accountability. In addition, DFC will determine appropriate public reporting of site visit data and report accordingly on a periodic basis.

Responsible Parties: Office of Development Policy; Office of Financial and Portfolio Management; Office of the Chief Development Officer; Office of the Chief Risk Officer; Office of External Affairs.

Target Resolution Date: 3rd Quarter of FY 2024

OIG Recommendation No. 8: Ensure all divisions update and finalize site visit monitoring policies and procedures to align with the agency's strategic goals.

Management Response: DFC concurs with this recommendation. DFC offices with a project monitoring role will update their respective site visit policies and procedures for alignment with strategic goals established for site visit monitoring.

Responsible Parties: Office of Development Policy; Office of Financial and Portfolio Management; Office of Equity and Investment Funds; Office of Development Credit, Mission Transaction Unit; Office of Structured Finance and Insurance; Office of the Chief Development Officer; Office of the Chief Risk Officer; Office of External Affairs.

Target Resolution Date: 3rd Quarter of FY 2024

OIG Recommendation No. 9: Develop a system to centrally track site visit reporting results that is accessible to staff for cross-monitoring purposes. The system should facilitate the formal sharing of lessons learned and trends identified during site visits for all phases of DFC's investment decision-making.

Management Response: DFC concurs with this recommendation and will develop and implement policy, procedure, and system changes to facilitate this recording and sharing of information.

Responsible Party: Office of Information Technology

Target Resolution Date: 3rd Quarter of FY 2024

OIG Recommendation No. 10: Conduct an internal workforce assessment of the Office of Development Policy to determine the appropriate current and future staffing needs and budget resources to perform site visit monitoring to assess Environmental and Social compliance and development impact.

Management Response: DFC concurs with this recommendation and will complete an analysis of current and future staffing needs within the Office of Development Policy.

Responsible Party: Office of Development Policy

Target Resolution Date: 2nd Quarter of FY 2024

OIG Recommendation No. 11: Develop a system to track all significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments.

Management Response: DFC concurs with this recommendation and will develop and implement a system to track these events.

Responsible Party: Office of Development Policy; Office of Information Technology

Target Resolution Date: 2nd Quarter of FY 2024

OIG Recommendation No. 12: Report significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments to DFC's Board of Directors and report such incidents in the Annual Report.

Management Response: DFC concurs with this recommendation and with the OIG's reporting that none of the mentioned environmental and social events were related to a lack of adherence to DFC's contractual commitments. However, to improve reporting and transparency, DFC will institute processes to report such data to the Board of Directors and in the Annual Report.

Responsible Parties: Office of Development Policy; Office of External Affairs

Target Resolution Date: 1st Quarter of FY 2024

OIG Recommendation No. 13: Revise relevant policies and procedures to better define how significant environmental and social events (fatalities and serious injuries) related to lack of adherence to DFC's contractual commitments impact DFC's monitoring site visit priorities, annual plans, and/or schedule.

Management Response: DFC concurs with this recommendation and will articulate in policies and procedures how these events impact the agency's approach to site visit monitoring.

Responsible Party: Office of Development Policy

Target Resolution Date: 1st Quarter of FY 2024

/s/

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Appendix VI: Glossary of Acronyms and Abbreviations

Table 4 contains definitions of all acronyms and abbreviations used in this report.

Table 4: Acronyms and Abbreviations

Acronym	Definition
BII	British International Investment
BUILD Act	Better Utilization of Investments Leading to Development Act of 2018
CDCS	Country Development Cooperation Strategy
CDO	Chief Development Officer
CEO	Chief Executive Officer
CRO	Chief Risk Officer
DCA	Development Credit Authority
DFC	U.S. International Development Finance Corporation
DOS	Development Outcome Survey
EO	Executive Order
E&S	Environmental and Social
ERM	Enterprise Risk Management
ESPP	Environmental and Social Policies and Procedures
FY	Fiscal Year
GAGAS	Generally Accepted Government Auditing Standards
GAO	U.S. Government Accountability Office
GoI	Government of India
IFC	International Finance Corporation
IG Act	Inspector General Act of 1978
IMML	Impact Management, Monitoring, and Learning
IQ	Impact Quotient
MSME	Micro, Small, and Medium Enterprises
MW	Megawatts
OCRO	Office of the Chief Risk Officer
ODP	Office of Development Policy
OIG	Office of Inspector General
OMB	Office of Management and Budget
OPIC	Overseas Private Investment Corporation
RMA	RMA Associates, LLC
SME	Small and Medium-Sized Enterprises
USAID	U.S. Agency for International Development
U.S.C.	United States Code
Xinjiang	Xinjiang Uyghur Autonomous Region