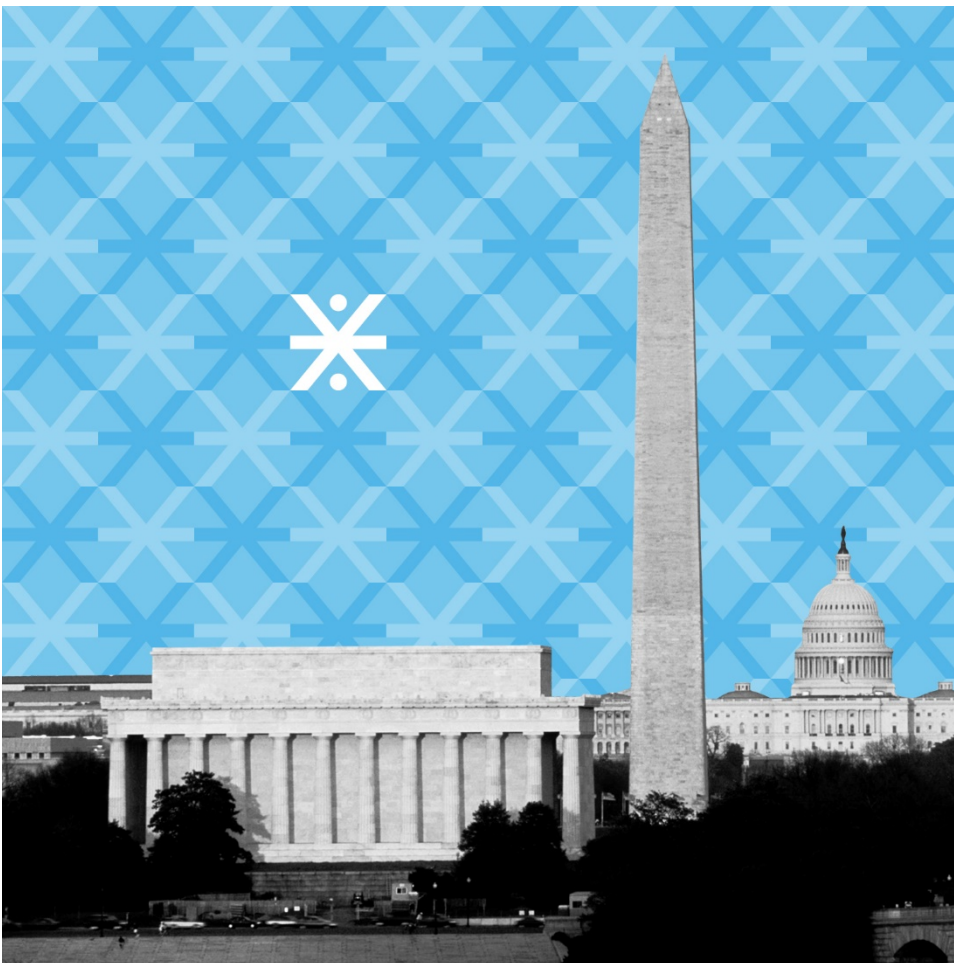


Best Practices to Evaluate and Update Risk Assessment and Credit Subsidy Capabilities for Federal Credit Programs

White Paper



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Objective

For more than ten years, Summit Consulting, LLC (Summit) has supported the agencies that manage federal credit programs per the requirements set forth in the Federal Credit Reform Act of 1990 and the Office of Management and Budget (OMB) Circulars A-11 and A-129. These requirements include the production and maintenance of tools used to assess credit risk. Common tools federal credit programs use include risk rating tools, scorecards, credit subsidy models, and recovery estimation methodologies. This white paper describes the tasks for which an agency can best leverage contractor support to enhance its risk assessment capabilities.

Description of Tasks

Should the agency deem it appropriate, contractors can review existing tools, design and implement updates to these tools, train its staff to use the updated tools, and provide ongoing support assessing risk.

Planning and Development Meetings & Work Plan

The contractor should facilitate meetings with a Technical Working Group (TWG) comprised of key personnel from the agency. The TWG works closely with the contractor to provide information and guidance for the development of the credit program's risk assessment tools. The TWG and the contractor meet regularly to discuss the status of tasks and deliverables, considering each task and/or deliverable described below separately and in sequence. Not all may be required.

*A **Technical Working Group (TWG)** is a committee of client leaders and staff that are most familiar with the needed uses of programmatic risk assessment tools, typically limited to three to five people.*

Review of Existing Tools

OMB Circular A-129 calls for periodic assessment of federal credit programs to identify efforts necessary to align their tools and process with their policy objectives and industry best practices. For each tool the program uses to assess credit risk, the contractor should perform a review to evaluate its features. As part of this review, the contractor compares the tool with corresponding tools used by similar federal credit programs. This review culminates in the production of a memo or report describing the current features of the tool, a comparison of the tools' strengths and weaknesses, and recommendations for retaining, improving, or replacing elements of the tool(s).

Design Documentation

Incorporating lessons-learned from the tool review, the contractor should facilitate discussions with the TWG to identify requirements for updated tools. Inputs to the discussions include requests from oversight bodies, the review of existing tools, and technical considerations. Based on the TWG's selections, the contractor compiles the requirements into a design document that will govern the tool's update. The design documentation should include the testing process for the updated tool, describing which tests the contractor will perform, and acceptable thresholds for testing outputs. This document may also include the level of effort needed to implement the updates, the justification for including specific requirements, and the documentation that will accompany the final tool delivery.



Model Construction, Testing, and Approval

The contractor creates the tool code conforming to the agreed-upon design documentation. Inputs will be in a format easily reproducible by program staff and will interact easily with existing systems. The contractor submits a draft tool to agency to provide feedback on the user interface and ease of use, including sample inputs, model code, outputs, and draft documentation.

After incorporating the agency's feedback on the draft tool, the contractor should conduct testing on the final tool. The design documentation sets forth the testing requirements, and the contractor documents results in a testing report. Testing can include usability testing, back-testing, sensitivity testing, stability analysis, and stress testing. The testing report should describe the testing methodology, testing inputs, testing results, and model updates resulting from the testing. Testing should also reveal the anticipated impact that the updated tools will have on credit subsidy reestimates, obligation subsidy rates, and portfolio management protocols.

The contractor should deliver full documentation with the final tool, as defined in the design documentation. Documentation can include methodology documents, user guides, data dictionaries, and standard operating procedures. The contractor should assist in producing analyses, memos, or presentations to support gaining approval for the updated tools from internal and external oversight bodies such as the inspector general or OMB. The agency may request that the contractor assist in presenting the updated tool.

Training

To facilitate a smooth transition toward use of the updated tool, the contractor should prepare training sessions and associated materials for program staff on risk assessment and credit subsidy estimation, with sessions devoted specifically to the updated tool. The agency may also require the contractor to provide training materials for briefing auditors and oversight officials.

Credit Subsidy Estimation Support

To promote adoption of the new tools, the contractor should assist the agency estimate credit subsidy rates for one or more seasons. For the President's Budget, the contractor should assist in preparing the necessary input files, operate the cash flow models, analyze and troubleshoot cash flow model error messages, provide validations of cash flow elements, and analyze changes in results from different cohorts. For financial statement and President's Budget reestimates, the contractor should assist with the calculation of the Financing Account Interest Calculation (FAIC), preparation of the reestimate cash flow model input files, data validations, operation of cash flow models, and analysis of reestimate results. The contractor should also assist in producing inputs and running the cash flow models for obligations and modifications, as appropriate.

Contractor Requirements

To complete the above set of complex and unique tasks and responsibilities, the agency needs access to contractors that bring demonstrated recent and relevant federal credit experience in the following competencies:

- Over seven years of experience supporting at least three distinct credit programs of similar description and complexity

- Recent and relevant experience designing similar tools for at least three distinct credit programs of similar description and complexity
- Demonstrated experience coordinating and conducting teaching/training. The provision of a training facility in the proximity of the staff and leaders who will operate the new tools is preferred
- Formulation of the President's Budget, to include:
 - Development, operation, and maintenance of credit subsidy models from a broad range of federal credit programs, including those that estimate credit subsidy separately per transaction
 - Strong familiarity with OMB Circulars A-129 and A-11
 - Financing Account Interest Calculation
 - Credit Subsidy Reestimation
 - Budget Year formulation, including support in completing the federal credit supplement inputs
 - Modification scoring in the event of a credit event
- Experience in auditing or validating the incumbent models being updated is preferred