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ACRONYMS AND ABBREVIATIONS

BOPS	Balance of Payment Support
CAS	Country Assistance Strategy
CEE	Central and Eastern Europe
CFAA	Country Financial Accountability Assessment
CIS	Commonwealth of Independent States
CPAR	Country Procurement Assessment Review
CPF	Counterpart Funds
DAC	Development Assistance Committee (of OECD)
DANIDA	Danish International Development Agency
DFID	Department for International Development
EC	European Commission
EON	Exchange of Notes
FOREX	Foreign Exchange
IASC	International Accounting Standards Committee
IFAC	International Federation of Accountants
INTOSAI	International Organisation of Supreme Audit Institutions
MOU	Memorandum of Understanding
NORAD	Norwegian Agency for Development Cooperation
OECD	Organisation for Economic Cooperation and Development
PER	Public Expenditure Review
SAI	Supreme Audit Institution
SIDA	Swedish International Development Cooperation Agency
SWAP	Sector-Wide Approach (see glossary)
TOR	Terms of Reference
UN	United Nations
UNDP	United Nations Development Programme
WB	World Bank

PREFACE

This report has been produced by two of Crown Agents' senior staff consultants, Mr Ron McGill and Dr Peter Boulding. The consultants conducted interviews with senior officials of (in the order of the terms of reference) Danida, Ireland Aid, The Netherlands Ministry of Foreign Affairs, Norad, Sida, DFID and KFW. Crown Agents acknowledge gratefully the assistance of all the individuals (listed in Appendix F) who were met by the authors in Copenhagen, Dublin, The Hague, Oslo, Stockholm, London and Frankfurt. Crown Agents remains responsible for all views expressed.

The description of the aid disbursement and accountability procedures of various donors has been based primarily on the documentation listed in the references below, but the report cannot replace the source documents as the definitive authority. Crown Agents has endeavoured to describe the main elements of the procedures accurately and comprehensively, but does not accept any responsibility for this report to be interpreted as a superior or alternative authority to the source documentation.

1 INTRODUCTION

1.1 THIS DOCUMENT

1.1.1 This report was contracted by the Department for International Development (DFID) on behalf of seven¹ donors. It follows a workshop² in The Hague in May 2000 when the commissioning of such a study was agreed as part of the follow-up action³.

1.2 TERMS OF REFERENCE

1.2.1 The detailed terms of reference are reproduced at Appendix A for ease of reference. The objective was to ascertain the scope, to identify the opportunities, and to recommend possible further steps for greater harmonisation of donor accountability requirements in the context of general (macro) and sector budget support. Focusing on commitment and disbursement of funds and reporting and audit arrangements for the donors that had agreed to participate (the study-donors), the TORs required, in summary:

- Review of existing procedures, including agreements between donor and recipient;
- Ascertaining the donors supreme audit institution's (SAI) position on accountability;
- Observations on assessment of recipient systems and institutions and the feasibility of common assessment criteria;
- Consideration of standards for recipients accounting and audit; and
- Comment on opportunities for greater harmonisation.

1.3 STUDY METHODOLOGY

1.3.1 The methodology followed has been largely that stipulated within the TORs (Appendix A).

- (i) A visit programme to the head office of each of the study-donor agencies. The personnel met were at the discretion of the donor, based on the suggestion that it should include aid policy, senior economists at the regional/country desks, internal audit, someone with familiarity with written operational procedures, handbooks or best practice notes and any other guiding legislation.
- (ii) The visit programme included a meeting with the SAI for each country.

¹ Danida, Ireland Aid, Netherlands, Norad, Sida, DFID, Germany.

² Donor Harmonisation and Adjustment of Financial Management and Control Procedures under Sector Programmes, Report on the Like-Minded Group Workshop held in The Hague, 25-26 May 2000.

³ Part III, section 2 of the report.

- (iii) Desk review of the documentation provided by the donor (written procedures/instructions and selected agreements between donors and recipient governments).
 - (iv) Review of relevant international auditing standards.
- 1.3.2 Prior to the visit programme two files were forwarded to the study donors, designed to act as a framework for discussion:
- A checklist that mapped the TORs to the project/programme lifecycle and provided a series of prompts for discussion. The various tables contained in this report have their origins in this questionnaire. Unfortunately, in only one or two visits was this questionnaire used systematically (Appendix B). Nevertheless, whilst the contents of the tables may, in certain places, be subjective or inaccurate, they will prompt the donors to answer them correctly; and
 - A graphic showing the generic flow of funds for programme aid (reproduced at Appendix C).
- 1.3.3 The documentation review part of the TORs was dependent upon the donors providing documentation. The volume and content of material provided was substantial but varied from donor to donor. Having received documentation there was an obligation that it should be reviewed, at least partially, even where the subject matter was, possibly, beyond the requirements of the TORs.
- 1.3.4 One of the ways that the subject has been considered during the study is to categorise the issues that might be constraints to harmonisation under three headings:
- (i) **Policy** – the will to adopt the “new paradigm” (a term used as shorthand throughout – see Glossary at Appendix D), the progress in development of policy and differences in policy perception.
 - (ii) **System** – the development of new systems to reflect the policy plus any inflexible procedural instructions and/or immutable donor government stipulations (e.g. treasury public finance guidelines). This was the main purpose of the TOR.
 - (iii) **Information** – this is wider than data flows; included here is common understandings and shared objectives, perceptions and attitudes, particularly at the embassy level.
- 1.3.5 Consideration under those three headings takes the study beyond the TORs. Whilst an attempt has been made to adhere to the TOR and methodology, in three areas this was not possible:
- The TORs call for a review of legal documents. It is believed that it is inappropriate to advise on the primary legislation that bears on the activity of donors. In the case of United Kingdom this would be a role for the Treasury solicitors. Only the UK primary legislation is discussed under the DFID country study (Appendix F), where an opinion is included; and
 - The relevance of many of the existing donor procedures to the new paradigm, of SWApS and/or macro-budget support, is questionable;

- The drift into the policy dimension beyond the mechanistic emphasis within the TORs. It is again questioned whether the harmonisation of procedures can be separated from the harmonisation of policy.

1.3.6 There appears to be a strong consensus on the developmental benefit of the new paradigm and most of the subject donors have moved their policy positions accordingly. They have also have reached various stages of development for new systems and procedures and have the issue of indicators under consideration. For these donors progress may make their existing accountability requirements, designed largely for project aid, redundant.

1.3.7 This quickly became apparent during the visit phase of the study. The concentration in this report therefore, is on the identification of any overriding constraint, (financial, procedural etc) that, despite a strong policy intention, might prevent a donor from co-ordinating its activity with other donors, participating in the pooling of funds, using recipient government systems and adopting a common position in terms of accountability and reporting arrangements. Further, an attempt has been made to extend the scope beyond just the current donor procedures towards the wider context, of co-ordination and harmonisation.

1.4 STRUCTURE OF REPORT

1.4.1 Many of the issues within the report are inter-related and there is no obvious structure that allows for easy presentation. The following paragraphs provide an overview to help readers follow the logic:

- (i) **Section 1** – Introduction: In addition to describing the purpose of this report this section summarises:
 - The terms of reference
 - Methodology
 - Report Structure
- (ii) **Section 2** – Background: this section attempts to put the study in context and includes reference to:
 - Glossary of terms (Appendix D)
 - Evolution of programme aid
 - A summary of a previous UNDP donor harmonisation initiative
- (iii) **Section 3** – Audit: this section looks at the audit issues and supreme audit institutions. It covers both donors (in terms of their responsibilities), and the recipients in terms of their accountability to the donor.
- (iv) **Section 4** – Donor Comparisons: this section draws some broad comparisons of the donors in terms of their current programme aid commitment and disbursement mechanisms.
- (v) **Section 5** – Other Findings: this section looks at the donors experience and progress towards adapting their approach and highlights some further change issues that have a bearing on progress towards enhanced co-ordination and harmonisation.

- (vi) **Section 6** – Assessment and Other Tools: within this section the issue of assessing the acceptability of recipients’ financial management systems is considered.
- (vii) **Section 7** – Case Studies - this section reviews some of the documentation provided by donors, particularly MOUs, that were not strictly relevant to that one donor. The review tries to give some insight into what has been happening and certain documents raise issues that are worth highlighting.
- (viii) **Section 8** – Other Harmonisation Opportunities.
- (ix) **Section 9** – Conclusions and Recommendations.

1.4.2 The individual donor studies are separated into an Appendix (Appendix F) and make reference to the documentation reviewed and the individuals met.

2 BACKGROUND

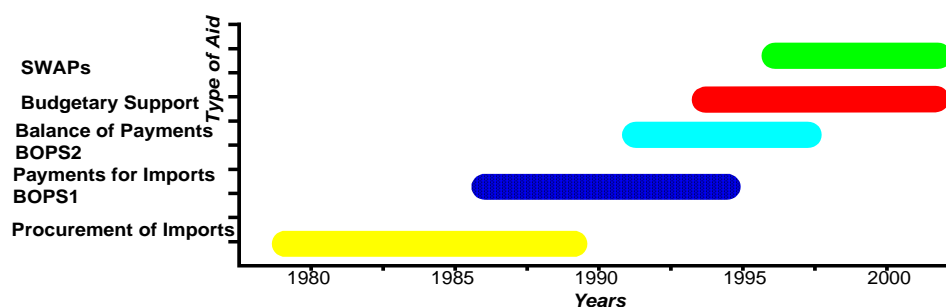
2.1 GLOSSARY OF TERMS

2.1.1 Before detailing findings it is worth setting the scene in terms of common understanding of issues. The issues are complex and open to debate, elucidation and refinement. However, much has been written on the subject[s] and it is unnecessary to include a discourse here. Instead, a limited glossary of key terms is appended (Appendix D), to put in context the statements contained herein and to demonstrate whether this report is in accord with a common understanding.

2.2 EVOLUTION OF PROGRAMME AID

2.2.1 It is also worth commenting on the evolution of programme aid, as it is informative in terms of the donors’ current positions for the new paradigm. Figure 1 illustrates how there has been a movement over time from micro-managed procurement of imports, through balance of payments support (BOPS) or commodity import support (in support of structural adjustment – principally forex liberalisation), including reimbursement of completed import transactions, to budgetary support. Budgetary support has, for certain donors, entailed resource transfer against a notional link with items of expenditure (such as teachers’ salaries).

Figure 1: Evolution of Programme Aid



2.2.2 All the study-donors have had resource transfers of this type, to varying degrees of volume⁴, although it may not have been recognised for what it was: budgetary support⁵. Arguably, the previous balance of payment and early examples of budgetary support had far less accountability than is now envisaged. There may have been some dialogue at budgetary level on the prioritisation of expenditure but not targeting of money towards supporting poverty reduction plans or the more specific targeting at sectors⁶. There were limited attempts to assess the government systems through which funds were channelled but no framework under which improvements to core government systems could be delivered.

2.2.3 So the question for this study is not so much: can the donors deliver resource transfers of this type (with questionable accountability)? They have been doing so. Nor is it so much: can donors co-ordinate their activity? More the question is: can the donors pool funds? Further, and largely beyond the scope of this study, the question is: what improved accountability can be agreed, or more pertinently, what different approaches to accountability can be devised?

2.3 PREVIOUS HARMONISATION STUDY

2.3.1 The problem of donors differing reporting requirements and the adverse impact on recipients has not newly been identified. As a result of UN meetings⁷ in 1989 and 1990 a working group was established to formulate ways to simplify and harmonise accountability requirements. In a three-year process and at a cost of US\$1.2M the study surveyed the accountability requirements of fifteen donors, looked at aid management and accountability issues within nine recipient countries and produced a framework consisting of ten basic principles⁸ (Appendix E).

2.3.2 After such an extensive initiative it has to be asked why the subject of harmonisation has made so little obvious progress and is still very much on the agenda for the study-donors and OECD/DAC? It is suggested that this is because:

- The study had too wide a focus;
- The consensus on developmental thinking (the new paradigm) was not fully formed (it was too early to bring about change);
- UNDP had insufficient influence on donors; and
- The initiative was redirected in focus (see paragraph 2.3.5 below).

⁴ In the case of Germany only under dispensation and low in volume. In the case of Sida there was a reducing volume trend for budgetary reasons rather than policy, with the trend now reversing.

⁵ In effect a disguised budgetary support but where the donors focused narrowly on the balance of payment deficit (and structural reform such as forex liberalisation) and paid little attention, if any, to the counterpart fund contribution to budget.

⁶ There were a number of cases where ceilings were placed on defence and floors set on social sector expenditure.

⁷ UN Expert Group Meeting on Government Financial Management in Least Developed Countries, Cyprus, November 1989 and UN Programme in Public Administration and Finance and INTOSAI, Vienna, 1990.

⁸ Report of the UN Department for Development Support and Management Services, Aid Management and Accountability Initiative 1991-1994, Int-92-801 DDSMS/SEM.96/2.

- 2.3.3 Notwithstanding, the study has increased understanding of the issues and the ten principles⁹ contain within them some of the thinking behind the greater consensus on development now achieved.
- 2.3.4 The initiative continues in the form of the UNDP's Programme of Accountability and Transparency (PACT), which has redirected and widened¹⁰ its focus to:
- Comprehensive public expenditure accountability (all sources of funds);
 - Anti-corruption/integrity improvement; and
 - Global networking, advocacy, policy development training, tools development¹¹ and national programme formulation.
- 2.3.5 Whilst this refocus has led to criticism, particularly of being done without proper consultation with recipient country stakeholders and those funding the programme¹², PACT would nevertheless appear to have relevance to the need to increase capacity in improving financial management, in areas of planning, budgeting, cost control, accounting, reporting and audit. It is understood that involvement beyond diagnostic has only been achieved in a few countries but the diagnostic tools may have relevance to the need to assess country capacity.

3 AUDIT AND EXTERNAL SCRUTINY

3.1 PURPOSE OF THIS SECTION

3.1.1 This section looks at the audit issues in a broad sense; internal, external and SAI audit. It covers both donors (in terms of their fiduciary responsibilities), and the recipients in terms of their accountability to the donor. Its main emphasis however, is on SAI issues, as required by the TORs.

3.2 AUDIT PRINCIPLES

3.2.1 The basic principles of financial and value for money (performance) audit are outlined below.

3.2.2 Financial Audit

- (i) Financial audit is the examination and review of accounting statements undertaken annually in order to form an opinion as to how faithful a picture they present of the financial activities of the entity. It may involve examination of financial management systems and the sampling of transactions. The ability for this to be carried out within a realistic level of effort pre-supposes that effective controls are already in place and a degree of internal audit is exercised. The concept of materiality is important in framing sample sizes and the evaluation of findings.

⁹ The ten principles are reproduced at Appendix E.

¹⁰ Including widening focus from initially anglophone Africa to Central and Eastern Europe (CEE) and the Commonwealth of Independent States (CIS);

¹¹ For country assessments of accountability and transparency (CONTACT).

¹² Danida and The Netherlands.

(ii) There are three relevant types of materiality:

➤ By Value

What would influence/be of interest to the reader of the accounts (parliament, public, press etc.) in terms of monetary size of errors encountered? As a very broad planning “rule of thumb” in the absence of other indicators, an estimate of 1 per cent of expenditure can be used.

➤ By Nature

This depends on the nature of the misstatement e.g. fraud or corruption could be material by nature at much smaller amounts than materiality by value. Parliamentary interest can be stimulated in relatively small amounts of money.

➤ By Context

Certain highly specialised figures have to be exactly correct to the last penny (e.g. figures appearing in more than one account and Consolidated Fund Extra Receipts).

(iii) There are seven standard audit objectives that relate to financial audit (NAO):

<i>Completeness:</i>	All transactions and balances relevant to the system in the period of account have been recorded;
<i>Occurrence:</i>	Recorded transactions properly occurred and were relevant to the period of account;
<i>Existence:</i>	Recorded balances represent valid assets or liabilities of the organisation;
<i>Measurement/ Valuation</i>	All transactions or balances are stated accurately and in accordance with generally accepted accounting principles;
<i>Regularity</i>	Recorded transactions are in accordance with relevant authorities, including treasury authority where required for specific transactions;
<i>Ownership</i>	Recorded balances represent assets and liabilities properly owned by the organisation;
<i>Disclosure</i>	Recorded transactions and balances are properly disclosed in the accounts in accordance with any necessary treasury directions, rules and generally accepted accounting principles.

3.2.3 VALUE FOR MONEY (Performance Audit)

(i) Value For Money (VFM) is a simple concept that has become pivotal to all aspects of public finance audit and management. In the UK it rose to prominence during the Thatcher government’s Financial Management Initiative in the 1980’s. Value for money audit developed at a similar time and focuses on measuring and evaluating the extent to which an entity achieves its performance objectives in terms of the three “e”s: economy, efficiency and effectiveness.

(ii) The three VFM elements are:

Economy, the avoidance of wasteful or unproductive expenditure - the extent to which an organisation minimises the resources it uses;

Efficiency, the maximisation of output relative to input - the extent to which an organisation achieves its objectives at minimum cost; and

Effectiveness, the extent to which an organisation achieves its objectives.

(iii) Value for money audit can employ a wide variety of methodologies in different circumstances. Value for money studies are often undertaken by supreme audit institutions. They may be highly focused, and can demand substantial inputs of time and resources to produce detailed reports for public and parliamentary scrutiny. Expertise utilised may include accountancy, economics and specialised consultancy. Value for money reports may, in some countries, result in public hearings of accounting officers in front of parliamentary committees (as such they are regarded as important public accountability mechanisms).

3.3 SIZE OF AID BUDGET

3.3.1 Before discussing the audit issues it is worth looking at a comparison of the size of the study-donors aid budgets (Table 1). This helps to set the context for the complexity of management faced by the donors and the degree of flexibility that they may exercise. The figures also help put in context the materiality of the programmes as viewed by the respective SAIs and the accountability to parliaments. There is an inevitable cross-over between issues discussed in this section and those that have a more donor focus:

Table 1: Comparison of Aid Budgets

	Denmark	Ireland	Netherlands	Norway	Sweden	UK	Germany
Value US\$ (Bn approx ¹³ ,1998)	1.70	0.20	3.05	1.32	1.55	3.83	5.59
Percentage of gnp	0.91	0.31	0.80	0.91	0.71	0.27	0.26

3.4 DEGREE OF EXTERNAL SCRUTINY

3.4.1 The figures however, are only part of the picture. They perhaps explain the current relative lack of materiality in the auditor general's office attitude to Ireland Aid's programme¹⁴. But they do not help illustrate the tradition of greater audit effort that exists in other cases (for example The Netherlands), nor the closer working understanding that appears to characterise Norad's relationship with their auditor general's office.

¹³ Source: OECD. The figures are approximate. They are also ODA and exclude NGO transfers. The purpose of inclusion is not direct comparison but the materiality because this has an effect on the degree of audit scrutiny. In this context the value figure will be viewed by auditors, rather than the percentage of GNP.

¹⁴ The C&AG's position on materiality may change as the Ireland Aid programme expands rapidly.

3.4.2 In any event the degree of external scrutiny experienced by donors is only partly a function of value. All donors can be subject to parliamentary scrutiny, in conjunction with or separate from national audit office scrutiny. Parliamentary scrutiny can be ad-hoc, unpredictable, inconsistent, idiosyncratic and/or have a political dimension. Further, there are the perceptions and attitudes of the tax-paying public. These too can be very variable depending on world events, media influences and relative well being arising from the performance of domestic economies. It has been generally believed that the public readily accepts project style interventions, whether of an emergency relief nature or a more general poverty relief. Understanding of the more complex development issues is seen as unlikely. In itself this is a disadvantage in presenting the new paradigm.

3.4.3 Against this background, in all the study-donors, there was an awareness of and care towards fiduciary responsibility. This went beyond the value of their programme and appeared to be independent of the immediate external scrutiny experienced. This is at the heart of the accountability issue: the degree to which the donors can embrace what they believe to be more developmental, without being seen to betray that trust.

3.5 LIKE-MINDED AUDITING

3.5.1 During each of the study visits, meetings with the supreme audit institutions were also undertaken. There were cultural differences between audit styles, approaches and structures and in the relationships between the parties but these were outweighed by the fundamental commonality of position between the audit institutions. Detailed differences between donor countries are presented in the country reports (Appendix F). This chapter summarises those findings.

3.6 AUDIT AND HARMONISATION

3.6.1 All the SAIs agreed unanimously that they were unable to make or challenge policy. Their role is limited to the examination of accounting records (financial audit) and, in most cases, some form of performance or value for money audit, i.e. examining the impact of policy through the economy, efficiency and effectiveness of provision. There is a “nice” distinction between the blanket prohibition on direct audit comment on policy and the permitted audit commentary on the impact or effects of policy (that may be interpreted as criticism).

3.6.2 It is up to the donor agency to set policy objectives and the means by which, on a case by case basis, each spend should be measured. It is against these that the audit institution may choose to judge the outcomes. The onus is therefore, on donor policy makers to set objectives that are sufficient, achievable and meaningful enough to achieve developmental outcomes but simultaneously not so unrealisable as to raise audit concerns. In this respect the donors’ audit fate is in their own hands. Ultimately, it is the accounting officer (the head) of the donor agency that is responsible.

3.6.3 The auditors were unanimous in being unable to provide comfort or “buy-in” in advance on the appropriateness of the new paradigm approach. The argument against provision of such advance positions is that it would compromise the ability of auditors to make audit opinion (potentially critical judgements), at a later date. The auditor is only able to make judgements on a case-by-case basis, usually on an annual or more infrequent time-scale.

3.7 RESTRICTIONS ON AUDITORS

3.7.1 Generally the auditors are parliamentary servants with their activities occasionally determined by parliamentary (or parliamentary committee) interests. This might result in the need to react to public interest that could go beyond public audit or policy logic and introduce an irrational but political element into the equation¹⁵.

3.7.2 The auditors of donor countries are strictly limited to auditing the funds of their own donor governments and the activities of their own institutions, such as embassies. There is no real means of audit of recipient government accounts, even though in all cases the right of access is sought within agreements. Once money has passed into general funds of recipients it becomes untraceable and therefore, not properly auditable. It has also been common practice to seek the recipient SAI’s audit or certification, although in many examples this has been either not forthcoming or represents something on which no reliance can be placed.

3.7.3 Some donors (notably DFID and the EC) have attempted to solve this dilemma by using an approach known as “continuous audit”, whereby real time checks are conducted and claims on grant proceeds are verified as they are raised. Under this arrangement disbursements are often matched against selected line items of expenditure. Whilst this is reimbursement it does confirm, at least, that specified or agreed priority expenditure has been funded in the immediate past (e.g. current financial year). It also gives incentive to the recipient government to continue with the priority expenditure. However, even this type of validation has been described as a “fig leaf” because of the notional link of the past expenditure to the current funding and because it is not comprehensive in its coverage in relation to the whole of the recipient government budget.

3.8 RELIANCE ON THE WORK OF OTHER AUDITORS

3.8.1 There was a high degree of unanimity on the issue of placing reliance on the work of other auditors, whether from other donors or recipient governments. Supreme audit institutions have specific responsibilities in relation to the audit of their own government’s funds and cannot abdicate that responsibility. They may place some reliance on the work of other auditors but fundamentally cannot delegate the mandate. They would still require sufficient assurance from their own investigations to certify national expenditure. It is necessary therefore, for there to be a certain level of examination (and perhaps testing) of third party audit activity before reliance can be placed. If the third party is the supreme audit institution of, say, a recipient country, it has to agree to reliance being considered and is entitled to refuse to participate on the grounds that its national supremacy could be undermined.

¹⁵ This view may not be fully shared. The Netherlands makes the point out that their auditors are independent in their activities and an irrational but political element should never be the case.

3.8.2 Informally it was recognised that in most cases there would be a willingness to consider placing reliance on the work of other study-donors SAIs, who would generally apply similar methodologies and risk analysis. Donor audit institutions are currently reluctant to place reliance on recipient SAIs because of perceived weaknesses and capacity/resource constraints, for example, some recipient countries have a very small cadre of qualified accountants/auditors.

3.8.3 Some donor SAIs¹⁶ were active in building capacity in recipient SAIs. In some recipient countries there is a grave need for capacity enhancement of the SAIs to maintain audit independence and integrity and good financial management practice (see paragraph 3.12 below).

3.9 INTERNATIONAL AUDITING AND ACCOUNTING STANDARDS

3.9.1 Given the supremacy issues discussed below (paragraph 3.10.1), the most appropriate minimum standards that could apply to recipient audit institutions are the recognised international auditing standards (such as INTOSAI or IFAC).

3.9.2 All donor SAI offices encountered were aware of and “signed-up” to INTOSAI standards. These standards (like all international standards) are the result of committee activity and bear the hallmarks of international negotiation and resolution. Despite these obvious shortcomings the INTOSAI standards provide an adequate basis for beginning an audit dialogue. As “guidelines” one auditor remarked that they represent the floor rather than the ceiling of aspirations. The current version of the INTOSAI Standards dates from 1995 and covers: Basic Postulates, General Standards, Field Standards and Reporting Standards of Government Auditing. They are currently under review.

3.9.3 International Federation of Accountants (IFAC) standards are perhaps most beneficially applied as accounting rather than auditing standards (given that IFAC's membership consists of national professional accounting bodies) but can apply to public auditing. IFAC standards cover six key areas of accountancy activity: auditing and related services, education, ethics, financial and management accounting, information technology and public sector accounting. Most of the world's major professional accounting bodies (representing 2 million accountants) are members of this New York based entity. IFAC standards are closely allied to accounting standards developed by its associate organisation the International Accounting Standards Committee (IASC), which is London based. There has been heated international competition for international prominence between the IFAC/IASC and an American standard setting institution. IFAC standards were only encountered once during the study, at the Dutch “internal” audit section, which undertook the financial audit of Dutch aid expenditure. In general, donor audit institutions were members of INTOSAI and preferred to participate in their standard setting and dissemination.

3.9.4 Given that most international auditing bodies subscribe to INTOSAI and aspire to achieve their standards it would seem sensible to continue their use for new paradigm reliance, with the proviso that they are basic minimum technical standards. Reliance should never be placed on the work of other auditors solely on the basis of adherence to international standards. Mutual understanding, possibly formulated during a working relationship that might include capacity building, is also important.

¹⁶ In particular the SAIs of the Swedish, Dutch (IDI-satellite programme) and Norwegians (Zambia).

3.9.5 A distinction should be made between international technical standards mentioned above and quality standards applied to their implementation. It is not proposed to review the quality standards literature here but suffice to say quality assessment techniques can be of value in assessing how far SAIs achieve or exceed international standards. International auditing standards need to be adopted and implemented by the recipient SAI but such measures to verify the quality, nature and degree of their implementation and the general professionalism within the institution, would require careful consideration in the light of international sensitivities. Great care has to be taken to avoid the de-motivational effects of overtly rejecting the quality of work of nascent SAIs in low-income countries. Nevertheless, see paragraph 3.12 below.

3.9.6 A list of African members of INTOSAI is included at Appendix H.

3.10 SUPREME AUDIT INSTITUTIONS

3.10.1 Supremacy of the audit institution is a critical issue. This has sometimes been overlooked by donors and recipient governments alike. It should not be possible to impose standards, requirements or any kind of restrictions on any supreme audit institution, which is by definition supreme. There have been instances where SAIs have refused to undertake work on behalf of donors because they were not consulted prior to the signing of formal agreements. This is particularly important in low-income countries where SAI resources may be severely stretched.

3.11 WORLD BANK INITIATIVE

3.11.1 The link between good governance and economic development is increasingly recognised as critical. James Wolfensohn, in his Presidential Address to the 1996 World Bank/IMF Annual Meeting, said that “Corruption is a problem that all countries have to confront. Solutions, however, can only be home-grown. National leaders need to take a stand...[and] governments that wish to fight corruption will over time attract the larger volume of investment”. This standpoint has led to a heightened sense of the importance of SAIs, with their crucial role in promoting the accountability and transparency of government that is the best safeguard against corruption in both donor and recipient countries.

3.11.2 It is understood that the outgoing Vice President and Controller of Personnel at the World Bank has written (July 2000) to INTOSAI (with a copy to all the SAIs) in a manner that is very critical of the status and standard of SAIs in the developing world. It has not been possible to obtain a copy of the letter. It may be a personal initiative but it is assumed that it is the start of an attempt to address shortcomings. This reinforces the question mark on the reliance that can be placed on the involvement of recipient SAIs by donors. Nevertheless, it is an initiative that could significantly move the issue up the development agenda.

3.12 SURVEY OF DEVELOPING COUNTRY SAIs

3.12.1 The Dutch auditors furnished a strategy paper¹⁷ for strengthening African SAIs. This contained a survey (Appendix H), of 23 African SAIs, resulting from several years of IDA financed assistance to SAIs in a number of countries. Both the strategy paper and survey make rather bleak reading. The report highlights:

- Lack of independence (reporting to a body other than parliament);
- Lack of professional standards (notwithstanding membership of INTOSAI);
- Lack of money (from a source that does not compromise independence); and
- Failure of government to act on findings.

3.12.2 The exception named is South Africa, where the SAI status has been transformed over five years, giving an example of what can be achieved, given sufficient political will. This has been partly achieved through an autonomous status rather in the manner of the creation of revenue authorities and revenue boards, except that the funding is also independent of the ministry of finance. The strategy recommends the addressing of the structural issues without which training and other measures would not be sustainable. It also lists actions designed to escalate the subject to Country Assistance Strategies.

3.12.3 The subject is of such importance in the context of the new paradigm (and within which a co-ordinated effort could be made), that these points are carried through to the conclusions and recommendations of this report.

3.13 AUDIT SUMMARY

3.13.1 The inescapable conclusion from visits to the supreme audit and other audit offices of the study-donors is that, with one exception, there are no insuperable audit barriers to more involvement in sector or general budgetary support activities and greater co-ordination and harmonisation of donor activity. This is because of the SAIs' inability to make or criticise policy. Auditors are able to give *opinions* on the impacts of policy, particularly on the economy, efficiency and effectiveness with which policy is implemented.

3.13.2 Although there was a general like-mindedness of audit opinion there were nuances of interpretation and differences in structure, resources and intensity of audit approaches. The presence, interrelationship and functions of internal audit also varied across the donors. There were also differences regarding reporting and institutional relationships. None of these issues impinge on the overall conclusion. Donor auditors' judgements are made in retrospect, on a case-by-case basis. They are therefore unwilling to "buy-in" to policy changes, such as support for the new paradigm, in advance. Ultimately the donors' audit fate is in their own hands and it is the accounting officer (the head) of the donor institution that is responsible.

¹⁷ Strengthening African Supreme Audit Institutions, A Strategy Paper and Action Plan, February 1998.

3.13.3 In terms of standards, INTOSAI has produced auditing and accounting standards that provide a basic minimum for general acceptance. These are general technical standards relating to the conduct of audit work. Despite some doubts as to their value (reflecting their committee-derived origins), they represent the best available practical framework. All the study-donor SAIs are members of INTOSAI.

3.13.4 The greater difficulty is in relation to recipient' SAIs and in deciding upon an objective assessment method to determine their progress in achieving these standards and, arguably more importantly, their general performance and professionalism.

3.13.5 Therefore, in considering whether it would be desirable, for the sake of simplicity, to agree minimum acceptable standards for recipient countries' audit institutions to enable reliance to be placed on their work (as required by the TORs), it has to be concluded that this would only address the issue in a limited way. There would remain questions of:

- (i) The sovereignty or supremacy of the audit institution. No external institution, international or otherwise, has the right to impose standards on a SAI. The SAI may decide to adopt international standards but may not be challenged as to its working methods. It may not be appropriate for a grouping of bilateral donors to challenge¹⁸;
- (ii) Who would actually determine whether or not a SAI is complying with the standards or achieving a sufficient level of professionalism? A possible solution to this might be if respected international agencies (such as the World Bank or IMF) would make their wider analysis of recipient government financial management institutions available for member nations to form a view on the results;
- (iii) Consistent failure to meet external expectations may have a de-motivating and damaging impact on the recipient audit institutions; and
- (iv) Each audit institution will have different political, economic, social and historical legacies. Thus each country would require individual solutions and "standards" would require tailoring to each situation.

3.13.6 It may be preferable to develop an on-going dialogue with the recipient SAI that involves a learning curve on both sides, enabling robust institutional support to be developed for the recipient and informing risk assessment by the donor community. This dialogue can be linked to the general governmental financial management dialogue that is a key part of the new paradigm.

3.13.7 In the following table (Table 2), the positions of the study-group are summarised. Although this section concentrates on the SAIs the first two lines relate to the donor position, the remaining to the donor SAI.

¹⁸ This does not mean that donors should disburse regardless of deficiencies, where standards are woefully inadequate donors can walk away.

Table 2: Summary of Audit Position

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Right of access	Yes	Yes But reluctant to exercise	Yes	Yes	Yes	Yes	Yes
Audit opinion required	Preferred	Annual	Preferred	Preferred	Preferred	"Continuous audit" alternative	Yes
Reliance on other donors and donor SAls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Reliance on recipient SAls	No	No	No	No	No	No	No
Donor SAI audit standards	INTOSAI	INTOSAI	INTOSAI	INTOSAI	INTOSAI	INTOSAI	INTOSAI

3.13.8 There is an apparent contradiction contained in the responses to the second point (Audit opinion required) and the fourth (Reliance on recipient SAls). It is suggested that this is because the response to the second point reflects a point of principle (as does the response to the first), whereas, the fourth is a recognition of reality.

4 DONOR COMPARISONS

4.1 PURPOSE OF THIS SECTION

4.1.1 This section draws some broad comparisons of the donors in terms of policy and procedure, particularly the current procedures and particularly for programme aid commitment and disbursement mechanisms. It attempts to highlight the differences where this has a bearing on their ability to participate (or participate effectively) in SWApS and budget support (and pooled funding thereto).

4.2 SEPARATE DONOR APPENDIX

4.2.1 More detailed donor comments are contained in a separate write-up for each donor at Appendix F. These are not an attempt to be definitive studies (as other more comprehensive studies exist¹⁹). Similarly, for the sake of brevity, previously available material on donor harmonisation has been excluded, such as that from the UNDP harmonisation initiative or, more recently, that produced for the workshop²⁰ in The Hague. Instead an attempt has been made to characterise the donors only with relevance to this study, using new or directly relevant material. In part, this Appendix F is used to demonstrate the volume of material that has been used to arrive at the conclusions. Inevitably, the relevance and comprehensiveness of this material was largely in the hands of the study-donors.

4.3 GENERAL POLICY FOCUS AND EMPHASIS

4.3.1 All the study-donors have a pro-poor, poverty reduction focus for their programmes with an emphasis on support to (primary) health and education. Similarly, there is a common interest in human rights, democratisation, good governance, rule of law, anti-corruption, environmental sustainability and gender issues – women in development. However, it is in the degree of emphasis for certain of these issues that difficulties for co-ordination could lie.

¹⁹ OECD/DAC.

²⁰ Donor Harmonisation and Adjustment of Financial Management and Control Procedures under Sector Programmes, Report on the Like-Minded Group Workshop held in The Hague, 25-26 May 2000.

- 4.3.2 For example, all donors take a general anti-corruption stance but Norad is considering a “zero tolerance” policy, which could have implications for their programme and their ability to co-operate. Similarly, German budgetary law would not allow any relaxation in probity. On the other hand, DFID has similar issues of governance and anti-corruption at the heart of their policy but this would not be as “zero-tolerance” but more that their whole programme would be characterised by considerations of governance and measures to bring about improvement over time²¹.
- 4.3.3 Issues such as an anti-corruption or human rights stance may not prevent donors agreeing an MOU and pooling funds but different judgements after a programme has started could threaten a carefully constructed joint donor position²². Inevitably, these judgements will differ and must be made in the light of the country specific circumstance.
- 4.3.4 Nevertheless, donor co-ordination goes beyond harmonised procedures and it may be that work on a series of principles that would guide such future judgements would help to promote greater cohesion of action in the event of serious developments. Some scepticism was expressed over whether such a code would cover any broad principles not already covered (by DAC) or whether a code could override the freedom to act politically in the light of circumstances. Would this infringement be desirable and/or likely to be successful? Nevertheless, it is submitted that there needs to be far greater common understanding and consensus on a range of issues, than currently exists. Further reference to a possible “code of conduct” is made elsewhere in the context of pre-MOU discussions and negotiation.
- 4.3.5 More fundamental philosophical differences exist. Whilst the German position is entirely consistent in terms of policy emphasis it is characterised by a distinction in the definition of development. In the German context this means investment; related to capital expenditure with the recipient meeting recurrent costs²³. The German view is that the recipients must be capable of meeting recurrent costs and the donors funds should be [viewed as] investment (additional). Continued external finance of recurrent cost would contain the risk that were it to reduce or cease the services would suffer and the investment would have failed. In strict terms however, under basket funding this distinction is lost. All donors would probably agree that donor funds should not create structural insustainability but attitudes to fungibility and additionality vary and the only way to address the difference may be within the MTEF and beyond to the poverty reduction strategy.

4.4 TYING

- 4.4.1 The issue here is whether tying rules constrain any donor from participation in the new paradigm (particularly pooling funds). Although the current policy positions (Table 3) within the study group, show some minor differences the issue would not appear to be an obstacle for any of them. If DFID’s position over the last several years is used as an example: in principle UK was tied²⁴ but the application of the tying rules had developed sufficiently with a waiver in place for programme aid that, in practice, it was not an issue for DFID when considering participation.

²¹ Nevertheless, for DFID extremes of poor governance, empirical evidence of corruption etc would lead to sanctions or withdrawal.

²² An example of this was seen in the different reactions to continued war between Ethiopia and Eritrea with Norway and the UK pulling out but the WB, The Netherlands and Ireland not doing so. Progress towards SWAp support was however, suspended.

²³ The issue is also one of sustainability with the German position being oriented to the productive economy, capital stock (but also social and economic infrastructure).

²⁴ The UK government has now untied aid with effect from 1 April 2001.

Table 3: Position on Tying

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Position for Programme Aid	Untied	Untied	Reciprocal untying for basket funds	Untied	Untied	Untied (from 1 April 2001)	Untied

4.5 MECHANISMS FOR COMMITMENT

4.5.1 Whilst differing in detail, the study-donors have very similar regimes for pledges, budgeting and formal approval for spends. All base a country programme on some form of periodic strategic analysis and make annual budget provisions in line with this analysis. All have an appraisal stage for particular spends. The degree of delegation to the embassies varies, which results in differences in terms of the need for and the detail of the headquarters review of an appraisal submission (programme design and issues of legal, financial, governance, procurement etc). Generally, a financial threshold dictates the need for submission to a formal review committee.

4.5.2 However, in the detail of these budget and commitment mechanisms there are significant differences that impinge on flexibility. The degree of delegation for the Netherlands (and to a lesser extent Ireland), allows the embassy to be very responsive, extending to The Netherlands’ embassies having the power of vires in budget line items.

4.5.3 Danida on the other hand must make case by case submissions to a parliamentary committee. Whilst this is routine with several hundred submissions annually, this inevitably impacts on embassy responsiveness. Similarly, KfW must make project submissions to four government ministries and could experience refusal if the submission is not seen as in line with policy (e.g. not sufficiently a development “investment”), even if this is very rare.

4.6 COMMITMENTS TO MEDIUM TERM EXPENDITURE FRAMEWORK

4.6.1 Planning and budgeting in a sector programme are heavily affected by the donor commitment process. It is crucial that donors recognise the importance of the timing of commitments in order to mitigate the difficulties in the recipients’ planning/budgeting process. There are several factors involved here:

- (i) At present all the study-donors operate cash accounting systems. Most experience considerable pressure to disburse within the time limits of cash constrained financial years because of the perceived negative implications of underspending on future budget allocations. The intention however, is to move to accrual accounting in the short to medium term (see Table 4). This will provide some marginal benefits in terms of the ability to transfer expenditure commitments across financial years.
- (ii) There is a multi-year dimension to this consistent with the MTEF process. There will need to be some progress on multi-year commitments (say for a three-year period). Donors will need to consider how their own budgeting process can facilitate these commitments.
- (iii) It is necessary that donor commitments for the next fiscal year are known about 8 months in advance to enable the state budgeting process to take its course²⁵.

²⁵ Based on Ireland Aid’s experience in Mozambique (PROAGRI and ESSP).

4.6.2 The key points of this section on commitment mechanisms are summarised in Table 4:

Table 4: Commitment Intentions in Advance

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Financial Year	1 Jan to 31 Dec	1 Jan to 31 Dec	1 Jan to 31 Dec	1 Jan to 31 Dec	1 Jan to 31 Dec	1 Apr to 31 Mar	1 Jan to 31 Dec
Movement to Accrual Basis	Medium term	Medium term	2 years	Medium term	Medium term	Immediate	Medium term
Multi Year Allocations	1	3	3 plus	3	3	3	3
Ministry[ies]/Parliamentary Approval (case by case)	Yes	No	No	No	No	No	Yes

4.6.3 It has been necessary to put a single figure in Table 4 against multi-year allocations. Whilst these figures suggest a great deal of flexibility it is believed the picture is not quite that clear cut. The Dutch country allocations have a three-year time frame but embassies can translate these allocations into commitments for individual activities for more than three years. Similarly for Norway: strictly there are annual appropriations from parliament but some flexibility is possible with most agreements being 2 to 3 years (or more). With Danida however, the parliamentary committee approval on a case by case basis may restrict them to a one-year commitment.

4.6.4 It is assumed that most donors allocate the budget to a single year account²⁶, which explains the pressures on year-end spend. However, all the donors have the ability to commit to long running projects where the cash-flow is (not necessarily) linked to a single year. It is assumed that this is based on treasury dispensation to categorise differently the budget for projects. It is questioned why therefore, were longer-term commitments to be part of the programme submission, multi-year (MTEF) budget could not be similarly approved. This may need further internal examination and discussion with treasury departments.

4.7 DISBURSEMENT MODELS

4.7.1 This requirement of the TORs under the heading of disbursement models has been interpreted as relating to the movement of funds, i.e. the currencies and accounts for the flow of funds and issues such as whether or not the donors allow commingling of their funds. There is something of timing, frequency and approvals within this subject but these issues have been dealt under commitment mechanisms.

4.7.2 The focus of this study is towards the donor procedures rather than the more variable country or programme specific arrangements. The country appendix outlines what information could be obtained from donors. This is summarised in Table 5 below.

4.7.3 The shift from project to programme aid has meant that the cash flow from donor to recipient is reduced from a large number of individual transactions for each component of a project (including direct procurement, payments or reimbursements), to either a single payment, or relatively few tranches of disbursement.

²⁶ Not the case with Sida: Sida has a general authorisation to allocate funds up to an amount corresponding to the overall budget for 3 years, excluding the present year. Sida does not have any formal pressure on year end spending. Any balance is brought forward to the following year.

Table 5: Disbursement Issues

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Use of agent bank	No	No	NIO optional	No	No	CAFSL	KFW is a development bank
Separate forex accounts	No	Flexible	MOF a/c held by central bank			Initially but will disburse to nominated account	Applicable in the context of disposition accounts
Separate CPF accounts	No	No	No	No	No	The practice but not essential	No
Exchange rate	Not stated	Not stated	Must be clarity on rate	Not stated	Not stated	Would expect published rate for day of transfer	Prevailing rate on date of disbursement
Timing of CPF transfer	Prompt	Prompt	Prompt	Prompt	Prompt	No stipulation but expect prompt	Prompt
Commingling of funds	Yes	Case by case	Yes But treated as advance	Yes	Yes	Yes	In certain circumstances
Receipt of funds to be acknowledged	No	Yes	Yes	Yes	Yes	No	No
Reimbursement allowed	Not applicable	Yes	Not applicable	If agreed by recipient	Not applicable	Yes. Normally seeks notional link	Yes
Interest accrual	Not applicable	Not relevant for direct transfer	Not a legal issue	Use of interest must be agreed	Not applicable	Not relevant for direct transfers	Only in the context of disposition accounts
Direct disbursements (e.g. to suppliers)	Not applicable	Might do so	Not applicable	Not normally but can be agreed	Not applicable	Not applicable	Yes

Currency

4.7.4 Whilst all the study-donors denominate a grant in the currency of the donor country²⁷, all of the donors are capable of disbursing to an alternative currency account (say US\$), by crediting the US\$ equivalent of a donor currency amount (Table 6). Alternatively it is assumed it would be possible to debit the cost of a stated (say) US\$ amount to the grant proceeds, subject to sufficient balance. This latter approach however, would carry risk and presupposes a level of commitment control that the donor may not be prepared to exercise for programme aid.

Table 6: Disbursement Currency

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Disbursement in Any Major Currency	Yes	Yes	Yes	Yes	Yes	Yes	Yes

²⁷ And some, like DFID, have a *preference* for disbursement in the donor country currency.

Flow of Funds

4.7.5 Whilst there are no general rules applied by donors for determining the arrangements, there is a generic model for the accounts and the movements of funds between donor and recipient, which applies regardless of the donor. This reflects the realities of the international currency and banking system and the usual relationship between a ministry of finance acting for the recipient government and their banker, the central bank. This model is illustrated at Appendix C, with the key to the main movements and relationships shown in an accompanying table.

4.7.6 In the context of programme aid²⁸ key features of the model are:

- (i) The central bank takes the donor proceeds into the country's foreign exchange reserves for which the central bank has the responsibility of management.
- (ii) From this point the donor loses sight of the foreign exchange proceeds of the loan/grant as the funds are commingled with all other sources of forex²⁹. Examples of donors trying to track forex beyond this point, or audit the use, are limited (although in some examples donors may expect confirmation of receipt of forex, require bank statements or insist that, at least initially, their forex goes into a separate account specially opened for the purpose).
- (iii) The central bank effectively purchases the foreign exchange from the MOF, generating local currency (counterpart funds – CPF).
- (iv) Typically, the equivalent CPF will be transferred into a MOF local currency account opened by the central bank for the purpose of the loan/grant, providing a limited audit trail for the movement of the CPF.
- (v) Thereafter, when the CPF are consolidated with the government accounts, in a similar manner to the forex, the funds become untrackable. The point at which this occurs varies, with some donors seeking to maintain the separation of these funds and agree their (future) developmental use.
- (vi) With very limited additions the generic model can be extended to provide a comparison with modalities for all types of aid fund (whether programme or project), without altering the basic structure (see step 7 at Appendix C).

4.7.7 Although in certain examples specific forex and CPF accounts have been set up, nothing from the study suggests that this generic model is not accepted by all the study-donors.

²⁸ Project funds can follow a similar model with some exceptions, for e.g. where funds may be transferred in advance of need for administrative convenience; e.g. the WB “special account” arrangement.

²⁹ And spread over different currencies with several correspondent banks in a number of accounts, with the main forex holding being in the currency of the greatest future liabilities (usually US dollars).

4.8 REPORTING

4.8.1 A great deal of discussion revolved round reporting requirements (and minimum accountability requirements). The discussion was inconclusive. This reflects that there are different requirements for SWAp and budget support, both of which are very different from the existing reporting requirements required for project activity. All the donors signalled a degree of flexibility. Some defined minimum requirements, which had their roots in financial accounting (paragraph 4.8.2 below), whilst acknowledging the shift to other measures. Table 7 attempts to record the position for each donor:

Table 7: Timing, Frequency and Necessity of Reports

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Minimum frequency	Annual	Not set in SWAp but quarterly	Trend to annual	Annual	Annual	No	Monthly
Disbursement against: <ul style="list-style-type: none"> ▪ Advances ▪ Retrospective 	Both	Both	Both ³⁰ (but potential audit problem)	Both	Both	Retrospective preferred	Xx
Statements of account	Yes	Yes	Yes	Yes	Yes	No	Yes
Forecasts for balance	Yes	Yes	Not specifically	Yes	Yes	No	Yes
Final report	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Audit report	Preferred	Preferred	Preferred	Annual or otherwise agreed upon	Preferred	No, continuous audit option	Yes

4.8.2 Ireland Aid gave an outline of what they believe would be desirable in a common donor position:

- Existence of Medium Term Expenditure Framework;
- Planning and Budgeting - work plans and budgets linking funds to objectives in the form of non-financial indicators;
- Disbursement Mechanisms - the linking of disbursement to previous period reports and work plans/cash flow forecast;
- Progress and financial reporting on at least a quarterly basis. Reporting should compare actual expenditure with budgeted expenditure for each planned activity; and
- Audit Arrangements (both annual and perhaps the need for interim reviews). The role and capacity of the Auditor General should be considered.

4.8.3 Norad defined the following as core:

- Progress report (timing to be agreed) to include progress/results in relation to plans and objectives/goals, budget against out-turn etc.;
- Expenditure (to date, as agreed) statement showing expenditure on programme in relation to amounts disbursed;

³⁰ The Netherlands has a preference for retrospective disbursement when the conditions are in place. As in most cases these conditions are not in place, advance payments still prevail.

- Accounts with proper audited statement; and
- Mid-term and final review.

4.8.4 This subject will obviously require further consideration by the donors³¹. Germany indicates that they believe it is appropriate that a minimum requirement is established. Most of the other donors indicated flexibility.

5 OTHER FINDINGS FROM THE STUDY

5.1 PURPOSE OF THIS SECTION

5.1.1 Since the study-donors current procedures (as covered by the previous section), may not be entirely relevant to the new paradigm, this section looks at the donors experience and progress towards adapting their approach. It conveys something of the nature of the visit phase of this study and also highlights some further change issues that have a bearing on progress towards enhanced co-ordination and harmonisation.

5.2 NATURE OF THE VISIT PHASE DISCUSSIONS

5.2.1 Before proceeding to detail these points it is worth commenting on the discursive³² nature of much of the discussion during the visit stage of the study. The word has negative connotations and it is not intended to imply lack of co-operation. On the contrary, without exception the reception was welcoming, hospitable and open. However, there was something roundabout and inconclusive about much of the discussion. Given the exploratory purpose of the visits this was understandable, partly. However, it is believed that it also reflected the:

- Complexity;
- Transition (change) process from previous forms of aid;
- Uncertainty of the “end-game”;
- Perception of risks; and
- Problems of how to square the fiduciary circle.

5.3 PROGRESS ON POLICY

5.3.1 It should be of no surprise that (with the possible exception of Germany³³), the will to proceed with the new paradigm existed amongst all the subject donors. It was striking just how unanimous. This is not to say that there are not doubts and confusions at certain levels within the organisations. But this will, extending into the political

³¹ At the DAC task force Harmonisation of Donor Practices – sub-group Financial Management and Accountability, and elsewhere.

³² Obliquely, round-about, tangentially, expansively, circuitously.

³³ Germany is ready to participate in SWAps and basket funding, not budget support.

dimension, is complete in terms of acceptance of the implications and determination to overcome the problems:

- In Norad’s case the approach accords well with a long held philosophy of recipient responsibilities and avoidance of intervention;
- With Sida the will has been formalised via instruction from government that acts as mandate for its pursuit; and
- In the Netherlands the new paradigm sits well with policy positions, on ownership of development programmes and in approaches to financial management and control, previously adopted.

5.3.2 Whatever the status of the aid department, the nature of its relationship to government or its approach to aid in the past, the will could not have been more complete and universal. However, this will has been translated into different levels of progress in implementation.

5.3.3 In terms of policy it has been articulated into intentions of varying completeness (Table 8):

Table 8: The Will and Policy Positions

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Clearly expressed will	Yes	Yes	Yes	Yes	Yes	Yes	No
Policy articulation	Partly	Started	Yes	Partly	Yes	Partly	No

5.4 ADAPTATION OF SYSTEMS

5.4.1 Most of the donors had formed working groups to bring about implementation, some with sub-groups that were examining issues such as governance, indicators or assessment tools. Whilst the policy articulation in some cases was advanced into guidelines, the missing ingredients (Table 9), were clear procedure, tailored model agreements and tools (see also section 6 below)

Table 9: Progress in Codifying SWApS

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Studies	Yes	Yes	Yes	Yes	Yes	Yes	Under way
Guidance material	Yes	No	Yes	Yes	Yes	Yes	No
Written procedures	Under prep	No	Part	Under prep	Part	Under preparation	No
Model agreements	Under prep	Use of precedent	Under preparation	No will use core requirement	Under preparation	Derive from written procedure	No
Appraisal and assessment tools	Under prep	No	Partially	Under prep		Partially	No

5.5 INFORMATION (AND UNDERSTANDING)

5.5.1 One surprising statement made during the study was that the burden on recipient was questionable and that the real burden was falling on embassies. This statement may have been deliberately thought provoking but it is clear that problems with the level of understanding, the capacity to handle and nervousness in implementation at the embassy level should not be underestimated. This may be compounded by:

- Actions being influenced by custom and precedent (largely project precedent);

- Lack of precedent for the new approach and lack of familiar guidance and procedures;
- Sector specialists having demands placed (input to forms of agreement, MOUs and accountability and conditionality issues), beyond their experience;
- The need for higher level analytical skills from head-office and embassy staff (for capacity assessments and judgements), rather than project management skills;
- Advanced decentralisation putting responsibility at embassy level where there may be reluctance (from lack of understanding – personal experience, shared perceptions/vision etc.), to take risks;
- Also at embassy level a possible heightened awareness of shortcomings in governance, concern over financial management or governments ability to deliver, given political realities;
- High turnover of diplomatic staff; and
- Inconsistencies between the project control paradigm and the new paradigm.

5.5.2 Not all the study donors may be experiencing all these issues or to the same degree but it is fair to say that this encapsulates the problems faced.

5.6 SWAPS COMPLEXITY

5.6.1 There was some debate as to the extra complexities within SWAps as opposed to macro-budgetary support. This extended to what appears to be a widely held belief that accountability complexities are heightened at the SWAp level³⁴ (rather than the macro-budgetary support level). It is certainly true that appraisal at the SWAps level can be more complex, partly related to the difficulties in defining the sector strategy/policy/plan. The reasoning in the sectoral context starts from the micro-level upwards, so as to ensure focus on structural poverty alleviation. There are also issues to do with measures and indicators that may not exist at the budgetary level. However, it is suggested that:

- (i) Heightened accountability concerns partly arise from a project control mind-set being carried “up” to the SWAp level.
- (ii) Macro-budgetary support and SWAps require similar assessments and a level of comfort with the government capacity and systems, because money disbursed at budget level is still finding its way through to the sector and district sector level.

5.6.2 Further, because of fungibility:

- (i) An emphasis on detailed sector accountability gives no more total safeguard than tight control is able to “ringfence” expenditure at the project level.
- (ii) Sector support also requires policy dialogue at the budget level.

³⁴ This was widely discussed. It is specifically mentioned in the Dutch guidance material: that a sound prior assessment of management capacity is seen as very important, more so for sector support than for budget support.

- 5.6.3 It is accepted that at the sector level it is possible to devise measures and indicators whereas at the budget level the scope may be too wide. It is also true that it should be possible³⁵ to survey service delivery at sector level.
- 5.6.4 Nevertheless, several donors expressed concern that it would be inconsistent to continue with exhaustive transactional controls at project level, whilst disbursing at a higher level with fewer (and at the budget level with no similar controls). Further, it is inconsistent in any one country to agree to disburse at the budgetary level, whilst determining at the sector level that the financial management gives unacceptable safeguards. In part the judgement at the budget level may be made on other criteria, such as macro-economic but the common accountability issues are inescapable.
- 5.6.5 Other donors expressed the view that the need was to increase the degree of accountability at the higher levels³⁶, rather than decreasing accountability at lower levels. The question is: what accountability measures at the higher levels? If the only safeguard at the higher level is from satisfactory government systems and these are acceptable at budgetary level then the need for greater (additional) accountability at SWAp level is questioned. This is not to dismiss donor-instigated checks at sector level (or district sector level), as these might provide audit lessons that would allow weaknesses to be addressed. Nevertheless, it is suggested that where budgetary support is being provided it is inconsistent to withhold from involvement at sector level owing to fears over accountability³⁷. Perhaps some clarity needs to be brought to this issue, as it is believed that the paradox is a block to harmonisation.
- 5.6.6 Finally on this question, it was suggested during the visit phase of the study that there is a need to de-link financial management (and accountability issues) from specific agreements and disbursement profiles and that there was a need to work on improvements to financial management on a parallel track³⁸. In a way this thinking is integral to the new paradigm where the ideal approach is seen as needing to:
- Take a long term view;
 - Remove conditions;
 - Avoid stop-go disbursement based on short-term perception of progress (although reserving sanctions); and
 - Seek incremental improvements and provide capacity building inputs over time.
- 5.6.7 “De-linking” therefore, can be seen as a particular way of describing this approach. It would not receive approval amongst all donors.

³⁵ And perhaps necessary, particularly with decentralisation, to at least sample that service delivery is reaching service consumers.

³⁶ Over that typically present for previous BOPs or commodity import support.

³⁷ Although it is accepted that support at budgetary level may also be justified by factors other than satisfactory accountability: macro-economic need, strong demonstration of the will to reform, pragmatic policy positions, improving trends, natural disaster, financial crisis etc.

³⁸ Whilst de-linking of in-year disbursements from specific financial management issues might receive broad support, few would agree that disbursement of budgetary aid should not take account of the performance of the recipient in strengthening its financial systems. This then becomes an issue of whether some donors would have an absolute minimum standard (make a judgement whether to disburse or not) or be prepared to disburse, seeking improvements over time.

5.7 TREATIES AND AGREEMENT MODELS

5.7.1 There is an important distinction in the nature of the formal, written bilateral arrangements, with some donors entering into legal contracts (or treaties), and others preferring a memorandum of understanding (MOU – to be distinguished from the joint donor/recipient - partnership - document covering the SWAp and hereafter the term exchange of notes - EON - will be used).

Table 10: Nature of Agreements

	Danida	Ireland	Netherlands	Norad	SIDA	DFID ³⁹	Germany
Use of Head Agreement ⁴⁰	-	Yes	-	-	Yes	No	Yes
Use of Treaty (contract)	✓	✓	-	✓	✓	-	✓
Use of EON style agreement	-	-	✓	-	-	✓	-

5.7.2 The following is a definition of the difference between the two, based on UK Foreign and Commonwealth Office guidance. The term “treaty⁴¹” describes an international agreement concluded in writing between states, which is intended to create rights and obligations in international law. An EON records international “commitments” but in a form and with wording which expresses an intention that is not legally binding. An EON is used where it is considered preferable to avoid the formalities of a treaty (e.g. where there are detailed provisions which change frequently or where a treaty requires subsidiary documents to fill out the details). Treaties are frequently subject to parliamentary ratification and are published.

5.7.3 The differences in approach however, may be more apparent than real owing more to semantics than real differences and it might be useful to invite the donors, via this report, to analyse why things are done in a certain way. Is it:

- Because that is the way it has always been done;
- A perception of the philosophy of approach that has a significance in a contractual sense; and
- Some constitutional legal reason why it must be done.

5.7.4 In case of Norad, it has been established that there are constitutional⁴² (and philosophical) reasons for the use of treaties. However, they have streamlined the process and avoided what might be seen as an administratively burdensome approach by those donors that adopt the EON approach. It is likely however, that differences will continue to exist and means must be found to minimise the impact of the differences.

³⁹ For Commonwealth countries, otherwise treaties apply.

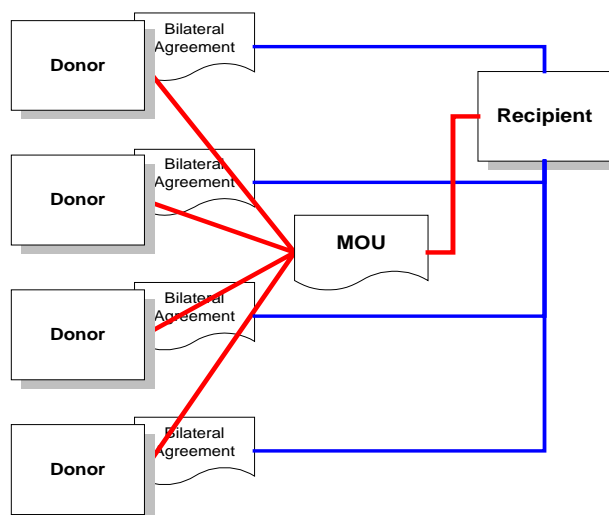
⁴⁰ An overall legal framework setting out the general terms and conditions under which the various support to the country (economic, technical and related assistance), is provided. Separate agreements would then be reached for specific items of support.

⁴¹ Known by a variety of names, e.g. agreement, convention, protocol, treaty etc. Confusingly, some treaties are also called MOUs or EON.

⁴² See Appendix F, section 4.

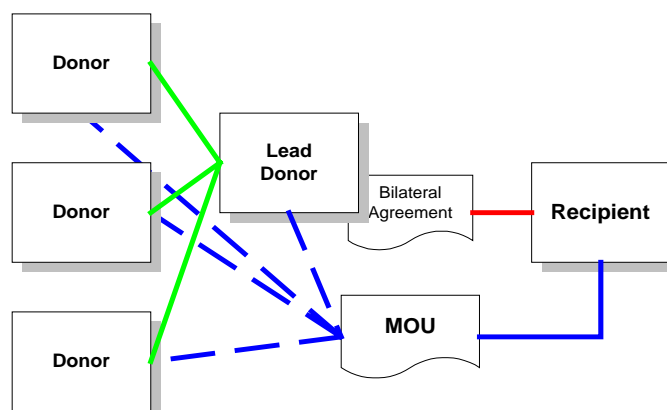
5.7.5 Illustrated are two models for the relationships between the parties. Figure 2 shows an MOU plus separate bilateral agreements. This is the most obvious model and has the advantage that the bilateral agreement will match with the donor’s usual practice (EON or treaty), with its timing dictated by the donors’ approval process. It would appear to allow more readily a unilateral termination or withdrawal. However, ideally the agreement should not contain additional accountability stipulations, conditionality or sanction measures that are not reflected in the MOU. In that circumstance the separate agreements are little more than the protocol of formalising the arrangements and should not be too administratively burdensome to the recipient.

Figure 2: Bilateral Arrangements



5.7.6 The second model (Figure 3), shows a lead donor and a single bilateral agreement. This has a similar effect to the first model but may be more appropriate where one donor has the obvious lead role in terms of in-country resources, sector specialisation and/or is contributing the greater part of the funds. It is possibly administratively easier (for the recipient at least) and the form of agreement and its stipulations (conditionality, accountability etc), can be based on those for the lead donor. However, the agreement should reflect a joint donor position, as contained in the donor sub-agreements. The lead donor may also need to consider their position should they enter into contract with the recipient but only have an EON type sub-agreement with a supporting donor[s].

Figure 3: Lead Donor Arrangement Model



- 5.7.7 There are other models. One to which attention was drawn (Nicaragua), was an example where it had been the intention for the recipient and all the donors to sign a single agreement (combining what in other circumstances would be MOU and treaty/EON stipulations). This has implications for those donors⁴³ who use EON rather than treaty. In this example the Nordic donors entered into one agreement and the Netherlands had to enter a separate agreement. It also has the potential to delay the overall progress if individual donors need to seek guidance on the (legal) content of the binding agreement.
- 5.7.8 The lead donor model also holds the potential for problems in the event of sanctions. Then the lead donor must decide their position. Most donors have general policy positions, which may bring about the lead donor taking a stance that does not reflect the view of one or more of the sub-donors. A donor code of practice would alleviate this circumstance.
- 5.7.9 Whichever way an MOU should not use the language of contract. The MOU is a record of understanding and even a statement of intention but its signature by the parties should not reflect a commitment by the donor before the donor is in a position to formalise this through an agreement (whether a contract or an exchange of notes).
- 5.7.10 Further, regardless of what type of agreement, it is important that all the donors apply the same set of procedures related to the support, monitoring and follow-up of the programme.
- 5.7.11 These are issues for co-ordination, which with operational autonomy delegated to the embassies could cause problems, at the least delays, for the future.

5.8 CO-OPERATION AND RELIANCE

- 5.8.1 Additional material on the issue of co-operation and reliance has been dealt with under the section on Audit (section 3, paragraph 3.8 above and Table 2).
- 5.8.2 Table 11 below is based on an interpretation of the visit discussions. It shows a very positive, co-operative position. However, it may be a bit subjective in content. The content could be subject to adjustment although it would be anticipated that the positive positions would be reinforced as the donors gain experience (and confidence) in working more closely.

Table 11: Summary of Position on Reliance

	Danida	Ireland	Netherlands	Norad	SIDA	DFID	Germany
Ability to act with other donors	Yes	Yes	Yes	Flexible	Flexible	Yes	Yes
Reliance on other donors, studies, assessments	Yes	Yes	Yes	Yes	Yes	Yes	With opinion of executing agencies
Ability to accept appraisal based largely on joint appraisal	Yes	Yes	Yes	Yes	Yes	Yes	With opinion of executing agencies
Willingness to work with lead donor agreement	Yes	Yes	Yes Policy Question Not Legal	Yes	Yes	Yes	With opinion of executing agencies
Willingness to channel funds through lead donor	Yes	Yes	Yes	Yes	Yes	Yes	Yes

⁴³ The Netherlands and DFID.

5.8.3 However, for the same reasons it is possible that this is an area where there could be inconsistency in circumstances of: different recipients, varying sets of donors and, even, the personalities of the individuals involved. More partisan issues of “voice” and desire for “influence” may undermine reliance and co-operation. It is certainly true that Norad and Sida, as an example, have a history of close working that might not be so readily replicated between a different set of donors.

5.9 CHANGE MANAGEMENT

5.9.1 This report makes several references to change management. It is not intended to comment on the subject at length, just to flag that most donors face a considerable task to adjust to what is intended. This is appreciated to varying degrees.

6 ASSESSMENT AND COMMON TOOLS

6.1 PURPOSE OF THIS SECTION

6.1.1 Within this section the issue of assessing the acceptability of recipients’ financial management systems (et al) is considered. A distinction needs to be made between a common assessment framework and the feasibility of consensus in terms of judgements and conclusions (the issue of common, core or minimum accountability/reporting requirements is discussed elsewhere in the report). The subject is expanded marginally to cover the potential for co-ordination of other tools used by donors that might aid co-ordination.

6.2 DIFFERENCES BETWEEN DONORS IN ASSESSING

6.2.1 It has not been possible to survey comprehensively in this area. Most of the donors are currently considering their position so differences are not apparent. They are in the process of developing analytical tools and checklists (see Appendix F), in order to:

- Give comfort of satisfactory capacity; and
- Identify the need for capacity building.

6.2.2 Examples are:

- (i) The Dutch have developed an Institutional Sector and Organisation Analysis (ISOA) and training material in the use of the analysis material;
- (ii) DFID have in draft a procurement capacity assessment which gives guidance on:
 - measures to counter corruption and examples of best (and bad) practice in procurement and a checklist to assist with diagnosis and
 - guidance for those involved in financial management analysis, particularly an intention to build capacity in financial management.
- (iii) KFW has fine-tuned over the years its project appraisal instruments for appraisal of project-executing agencies, which would allow a similar approach to the Dutch and DFID.

6.2.3 It is suggested that whilst the purpose of such tools may be the same they will be different in terms of content and approach (and, may it be said, in quality). There was every indication that the study-donors would be willing to pool experiences and share their tools. It would take quite an effort however, to take the best part of each and produce a set combining the best features. It might be more productive to:

- Agree in principle the need for and objective of each tool;
- Commission a best practice model; and
- Modify this to donors' satisfaction.

6.2.4 It is partly for this reason that it is argued at 8.5 below that the adoption of WB tools may offer the best prospect. Notwithstanding, donors must give their staff the guidance, if not to enable them to carry out the original analysis⁴⁴, then at least the wherewithal to guide their judgements, something that they alone must make. For this common tools may be less essential. Ultimately, and independent of the tool, it will be the quality of analysis that will be important.

6.2.5 Inevitably, and this could prove a paramount factor, there will be the variations in terms of judgement and conclusions arising from the analysis. Concurrence may best be served by starting from a common base methodology.

6.3 FEASIBILITY OF COMMON SET OF CRITERIA

6.3.1 Bringing together issues of assessment tools and financial management and audit standards, Germany has expressed the desirability of having a catalogue of questions containing a compilation of requirements for economically efficient budget management, to be observed irrespective of national legislation. They suggest this could follow, for e.g., the "Standards for Internal Control of the United States General Accounting Office or the examination of the reliability of management and economic efficiency under section 53 of the German budget law (management organisation, instruments and activities). Further they suggest the catalogue should also enable an examination of the organisational provisions to determine target achievement for development co-operative objectives. This suggestion would be of interest to the DAC Task Force on Procedural Harmonisation and/or the sub-group on Financial Management and Accountability.

6.3.2 The donors would appear to be prepared to share tools but the development of a commonly approved set would be a major task. It would also have to await each donor's determination of what is wanted. The reliance by donors on other donor's analysis would appear to be feasible (see Table 11). However, the recommendation would be for the WB to take a primary position using their range of diagnostic instruments for institutional and fiduciary issues (see paragraph 8.5 below).

⁴⁴ Although it is assumed that the WB in carrying out the role would seek inputs and contribution from bilateral donors.

6.4 COMMON TOOLS

6.4.1 The subject of “tools” is expanded marginally here to include the common appraisal, monitoring and evaluation tool, the *Logical Framework* (logframe). In several documents provided by the Dutch there is a reference to the Logical Framework as a planning and monitoring tool. These, inter-alia, note its usefulness when developing indicators⁴⁵. It is an effective tool requiring rigour and clarity. Whilst commonly adopted it has been implemented within many donors systems with varying degrees of success. This could be an obstacle to co-ordination, particularly where the terminology used and the internal guidance and training on the use of the tool differs from donor to donor. In the context of adopting common tools it is suggested that the logframe be included to ensure a consistent use across donors.

7 CASE STUDIES

7.1 PURPOSE OF THIS SECTION

7.1.1 In clarifying the TORs it was agreed that the focus should be the donor procedures, rather than expanding the study towards in-country experiences and recipients requirements⁴⁶. During the study, inevitably, it proved necessary to discuss real examples, particularly those that were current. There was encouragement from the study-donors to use some case studies to highlight particular issues.

7.1.2 Further, the study-donors produced a volume of documentation, ranging from country strategy papers, MOUs, agreements and ad-hoc studies and reports. All required to be reviewed. Although not all had relevance to the TORs their review did give some insight into what has been happening and certain documents raised issues that were worth recording. In order not to give undue weight to these issues the detailed findings have been removed to an Appendix (Appendix G). Abbreviated comment is retained in the main text.

7.2 VARIATION IN PURPOSE OF THE MOU

7.2.1 In the following paragraphs are highlighted some significant differences in the purpose and content of several examples of MOUs. These help to explain why a range of donors (including technical co-operation agencies), may be able to sign certain MOUs but not others. They also provide several examples that may be illustrative of some of the difficulties faced to date, including poor co-ordination and inconsistency in a donor’s position.

7.2.2 These are not meant to be case studies of SWApS but help to illustrate the variability and inconsistency within MOUs (for example where they included firm arrangements for basket funding and other procedural issues or where they just recorded the recipients intention to have a SWAp and the donors, equally broad, support to that.

⁴⁵ They note the usefulness of the logframe approach with regard to hierarchies of objectives: looking “down” to target groups at the micro level and looking “up” to objectives at the macro level.

⁴⁶ Which might have to be a further phase of study.

(i) **Zambia National Health Strategic Plan (14 April 1998)**

- Signed by six⁴⁷ of the seven study-donors plus several other multilateral and bilateral agencies⁴⁸, this MOU records broad understandings reached and indicates the partners broad acceptance of the move towards the concept of sector wide support, the vision of all resources being reflected in the MOH action plans and the ultimate vision of one basket of funds towards which all the partners would move *at their own speed*. It is therefore, a record of intentions rather than arrangements for specific funding.

(ii) **Uganda National Health Policy and Health Sector Strategic Plan (undated but year 2000)**

- Signed by most bilateral and multi-lateral agencies including the seven study-donors this document records Uganda's "commitment" to the health sector strategy and plan, to an increase in resources annually over five years and to partner consultation. It also commits the donors to synchronised review and monitoring, moving to the use of government systems and transparency in future plans for support to the sector;
- Partners are to work towards use of the government procurement procedures. Without being specific the MOU goes on to state "taking into account the legal obligations of the development partners". This suggests doubt or reservations on the part of some the donor participants about what they may be allowed to do.
- In addition to periodic external audit the MOU states that the MOH shall be audited by the Auditor General annually. This document is not a legal commitment and it is not known if this was cleared by the Auditor General.
- Funds are earmarked to health and ring-fenced at treasury but how individual donors might disburse to this arrangement is not clear. Similar, to the Zambia MOU this is a record of intentions rather than arrangements for specific funding. It throws little light on any of the subject donors policy and or procedures.

(iii) **Tanzania Prioritised Plan of Action for the Health Sector for the Financial Year 1999/2000⁴⁹**

- This MOU represents a different stage of co-operation. It clearly defines the transition to the SWAp. It also differs in that, rather than just record some basic principles related to the SWAp (the governments role, co-ordination arrangements etc.), it makes specific reference to:
 - Prioritised action plans and budgets

⁴⁷ Not Norad, and the German signatory was GTZ (technical cooperation), not KFW.

⁴⁸ EC, IDA, JICA, UN Children's Fund and UN Fund for Population Assistance, USAID and WHO.

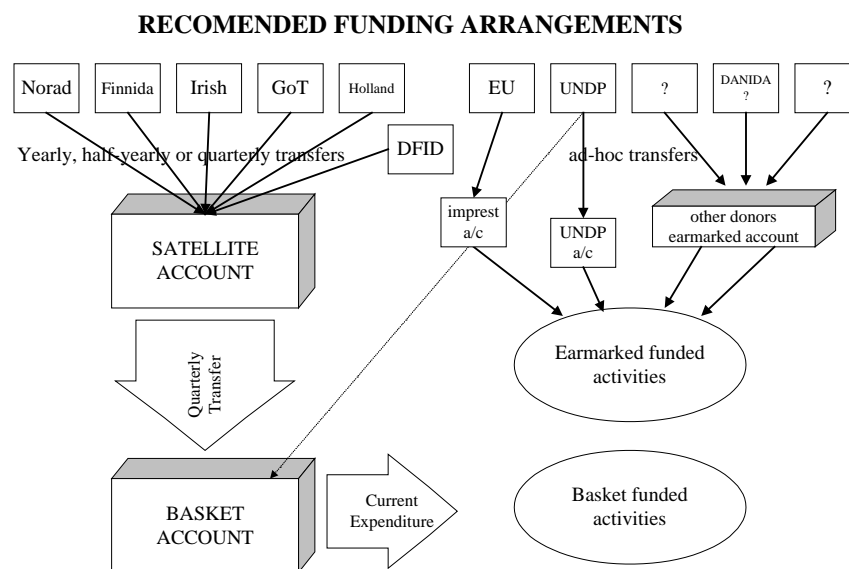
⁴⁹ Memorandum of Understanding between The Partners (Government of Tanzania and Donors - Danida, DFID, Irish Aid, Norad [and SDC and the WB]).

- The basket funding arrangement (US\$ holding account, consolidated fund)
- The accounting manual⁵⁰ (joint disbursement) and government financial regulations
- Procurement arrangements
- Reporting arrangement
- Audit arrangements (TORs)

(iv) Tanzania Local Government Reform

- In a similar fashion (to paragraph 7.2.2(iii) above) a fourth MOU⁵¹ is also a much more specific SWAp management agreement. It also makes specific reference to the funding of the programme, and the programme’s financial management manual.
- It is interesting to reproduce Appendix 15 of this latter document (Figure 4) and to ask why the different donors, particularly the study-donors, should adopt different disbursement mechanism when this study can find no reason (for the study-donors at least), not to join the basket? It is suggested that this is related to various country and circumstance specific reasons and not to overriding donor procedures or constraints:

Figure 4: Tanzania Local Government Basket Fund Model⁵²



⁵⁰ A review of the accounting manual has not been possible, as this would be significantly beyond the TORs.

⁵¹ Memorandum of Understanding between the Government of the United Republic of Tanzania and donor governments [which?] supporting the Local government Reform Programme.

⁵² Although attached to the Financial Management Manual and provided by Ireland Aid for this study (Embassy of Ireland Dar es Salaam, 5 October 2000), it is not known if this is the current status of the basket fund. Nevertheless, the model is a useful illustration of differing approaches by donors.

(v) Mozambique Macro Finance

- This example of budgetary support was emerging at the time of the visit phase of this study and was used as an example for discussion. Several points emerged:
 - The draft contained the language of contract, which proves difficult for the Netherlands and DFID. It contains not only a record of understanding and procedural rules but wording committing donors, e.g.:

*Quote: “following...the donors **will** make commitments” and “...**will** work to strengthen the state audit...” unquote.*
 - It also contains a stipulation that the SAI will provide an audit statement. This has the potential, were the Mozambique SAI to fail to meet the MOU requirements, to create difficulty with the donors’ SAIs.
 - More significantly it provides an example of several donors being prepared to disburse budgetary support via a financial management system of known weakness. The draft MOU is an example of an MOU with the least conditionality, performance measures or reporting requirements. It is understood this was deliberate for the reasons that the poverty action plan had not been finalised and the lack of performance measures gave the donor signatories the most flexibility in monitoring, with implied sanctions if not specific conditions.

(vi) Nepal Education

- Norad provided a report on an education programme in Nepal⁵³, which examines the setting of objectives and the use of performance indicators. It provides a useful example of lack of co-ordination. The report asks: quote “...if it is absolutely clear to all donors and to the government of Nepal by which objectives and indicators the co-operation will be measured[?]”. Three annex were attached to this report, which highlighted the differences within the programme documents and the donor agreements.
- The date, history and gestation of this sector programme are not known. It is assumed that the donors arrived at their positions (and drafted agreements) independently. The last annex is attached in Appendix G to this report as an example of how donor co-ordination should not be. This has implications for accountability because, almost certainly, the government would fail to satisfy one, some, or, more likely, all of the donors. An audit report on such a programme would be certain to find shortcomings and poor value for money in the aid spend as measured by the donors’ own criteria (despite any real improvements that might have been achieved by the programme).

⁵³ Basic and Primary Education Program II (BPEP II), Nepal.

8 FURTHER HARMONISATION OPPORTUNITIES

8.1 BUDGET ANALYSIS

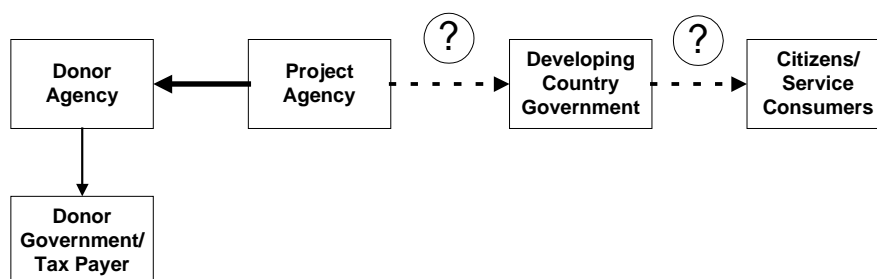
8.1.1 The Dutch highlight that this issue probably deserves more attention than it has been given. Certainly the issue of fungibility makes budget dialogue an essential element of the new paradigm. They propose a historical analysis of budgets and annual reports and annual accounts to reveal a trend in budgeted and actual expenditure.

8.1.2 Many donors highlight the need for attention to the out-turn (not just the budget), as part of a continuous and year on year monitoring process. Further, the out-turn can give indication that the actual expenditure reflects the total resources available, giving some comfort, at least at a high level, on the use of donor contributions.

8.2 WIDENING ACCOUNTABILITY

8.2.1 Up to this point this study has used a rather narrow, one-way definition of accountability. This is consistent with the traditional aid relationship with the recipient project agency being responsible to the donor agency (Figure 5):

Figure 5: Traditional Aid Accountability



8.2.2 In a “think-piece” commissioned by the Canadian Development Agency (CIDA) to stimulate debate, Mark Schacter developed a position⁵⁴ that to some degree, “turns this on its head”. This posits that donors must:

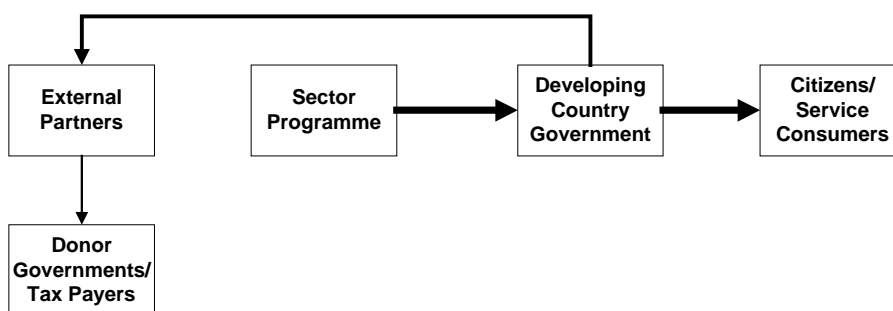
- Abandon the pretence that they can hold themselves *directly* accountable to the public for development outcomes in the countries they support;
- Adopt ways of reporting that acknowledge there is *no* causal link between donor input and development outcomes; and
- Acknowledge that the primary concern is *not* accountability by the developing country to the donor.

8.2.3 This thinking may not be entirely new to other donors but it may be difficult to embrace. It does however, reinforce the idea that SWAps design must build-in governance knowledge and expertise. It particularly throws focus on the broader question of accountability and governance within the country. By shifting the locus of accountability to the core institutions of the developing country there is a significant change in the direction and, potentially, the quality of accountability relationships⁵⁵ (Figure 6).

⁵⁴ With acknowledgement to: Sector Wide Approaches, Accountability and CIDA: Issues and Recommendations, Mark Schacter, Institute on Governance, October 2000, revised January 2001.

⁵⁵ More fully the paper argues: “There is an important distinction between managing for development results and being accountable for showing that inputs have been the direct cause of development results. The

Figure 6: New Accountability



8.2.4 This moves to a situation from where the donor is the focus of accountability to where:

- The donor and recipient government are jointly accountable for the success of the SWAp; and
- The recipient government is accountable *to its own people*.

8.2.5 The idea of measures to increase government’s accountability is not new. It has been suggested elsewhere in the context of SWAps that donors should do more to involve civil society and the private sector but it has also been suggested that care needs to be exercised to ensure that this involvement does not become unwieldy. Nevertheless, there may be other ways that this can be done, such as:

- Increasing the transparency of government; and
- Raising awareness and service expectation.

8.2.6 Certainly, this type of thinking alters the risk relationship between donor and SAI but does not necessarily answer the donor concerns on parliamentary/political scrutiny, protect the donor from media manipulation, nor ease the presentation to taxpayers.

8.3 DONOR CO-ORDINATION

8.3.1 There appears to be some uncertainty about how donor co-ordination at the country level is structured and organised. Partly its effectiveness will have something to do with the participants and personalities involved at the embassy level. The capacity at this level was an issue frequently referred to during the study and it may be that head office support to co-ordination, possibly at the early and last stages of the formation of an MOU, would help to establish the co-ordination.

8.4 DONOR CODE OF CONDUCT

8.4.1 Mention has been made elsewhere (paragraph 4.3.4 above) of the need for a donor code of conduct. By this is meant the development of a set of principles that will guide donors in the new more collective responsibility and in their judgements and in reactions to circumstances. Its application could be two-fold:

SWAp, with its emphasis on shared accountability and multi-partner collaboration under the umbrella of developing country leadership, highlights this distinction. The developmental goals of the SWAp are not consistent with attempts to attribute particular development results exclusively to the donors own inputs”.

- (i) Prior to signing to SWAp involvement;
- (ii) During implementation and particularly for use during the consideration of sanctions.

8.4.2 It is beyond these TORs to develop these but some thoughts are included to demonstrate what is meant. These may be thought to be obvious but may trigger debate and further development:

- (i) Donors “signed up to” the full implications of the new paradigm and its totality as a paradigm;
- (ii) Partners will operate with transparency;
- (iii) No unilateral suspension of funding without full consultation with all partners;
- (iv) In the event of outbreak of war that the expected determination (following consultation) will be the suspension of disbursement of fungible funds (in this context suggested as budget and SWAp funds disbursed through government systems, whether or not basket), that could be used to extend the attrition of war;
- (v) Whilst within the new paradigm the failure of conditionality in the past has been acknowledged this does not mean that sanctions must never be invoked;
- (vi) Conditionality related to the recipient government acceptance of the need for improving trends in management and governance is paramount;
- (vii) Measures to enhance the independence and effectiveness of recipient country SAIs will be an essential component of this approach;
- (viii) Guidance on what “voice” or influence a donor may have depending on the financial contribution or the disbursement model selected (aimed at circumstances where donors have signed MOU but have not contributed funds, or have been excluded voting rights within co-ordination committees because they have not pooled funds).

8.5 ROLE OF THE WORLD BANK

8.5.1 It is understood that the WB has made a policy decision to use adjustment lending rather than investment lending for their involvement in SWAps and budget support. This will make a substantial difference to their ability to become involved jointly with bilateral donors and the rules under which they participate.

8.5.2 Most of the study-donors have identified the greater analytical work required for the new paradigm and have started the process of training staff and developing assessment tools. However, in circumstances of several donors funding a budget or a sector there is a limit to number of detailed assessments that can be performed. Clearly the responsibility for decisions on when and in what form to grant funds rests with the donor but the study has found that donors, in addition to being prepared to share tools (see paragraph 6.3.1), would be prepared to place reliance on assessments of other parties (paragraph 5.8 above), assuming they are satisfied with the quality of the review process.

8.5.3 For assessments to be of true value they would need to have a number of characteristics:

- Thorough and comprehensive;
- Structured and systematic;
- Diagnostic and contribute to plans for strengthening; and
- Be cyclical in nature in order that improving trends can be determined (or more negatively in order for a deterioration in standards to be identified).

8.5.4 The WB's technical background note that formed their written contribution to The Hague workshop highlighted their move to a more systematic assessment of recipient accountability, through increased attention to governance and corruption. It stated that Bank and donor programmes must be grounded in the assessment of, and reform of a country's systems and institutions and listed the diagnostic instruments for institutional and fiduciary issues:

- (i) Public Expenditure Review (PER) – the assessment of revenue and expenditure management institutions is expected to become an increasingly important component of PER work.
- (ii) Country Procurement Assessment Review (CPAR) – to be enhanced.
- (iii) Country Financial Accountability Assessments (CFAA) – this is a diagnosis of a country's private and public financial management systems. Its purpose is to help a borrower assess and manage the risk that public funds will be used other than for agreed purposes (fiduciary objective), and to support the borrower in the design and implementation of financial capacity building programmes (development objective).
- (iv) Country Profiles of Financial Accountability (CPFA) – designed to promote dialogue on the reforms necessary to public procurement and general commercial environment.
- (v) Country Policy Institutional Assessment (CPIA) – measure the quality of budgeting, financial management, transparency, accountability and corruption.
- (vi) Institutional Governance Reviews (IGR) – broad gauge assessment of the quality of accountability, policy making and service delivery.

8.5.5 It is understood that a separate study is looking at the assessment of recipient's public financial management systems⁵⁶ and is likely to recommend that donors use the WB's CFAA as the basis for common assessment and that this be used by recipient governments to develop a programme of systems improvement, supported by donors. Performance against such a programme could trigger shifts in the proportion of donor resources transferred through recipient government systems.

⁵⁶ Part of the work of the SPA task team on public financial management.

8.5.6 It is suggested that substantially the best option is for the WB to take the primary role⁵⁷ in assessment of government capacity and benchmarking the need for improvement and measuring improvement over time. This would include, inter-alia the CFAA for the accounting side of the financial management equation. This is not to say that the donors should not continue development of the analytical tools necessary for their own processes and judgements, just that there would appear to be room only for one comprehensive, systematic and cyclical assessment regime. This should include an improved procurement capacity assessment (CPAR).

9 CONCLUSIONS AND RECOMMENDATIONS

9.1 BROAD CONCLUSIONS

9.1.1 There has been nothing revealed within this study that suggests the study-donors⁵⁸, may not participate fully in (progress towards) the new paradigm. Indeed, they are already doing so. This is not to say that there are no controls on their actions. On the contrary, depending on a combination of value and sensitivity these controls escalate the review of the donor activity up to the highest management level and, ultimately to the political level.

9.1.2 It is here however, that the will to proceed with the new developmental thinking exists. The convergence of thinking amongst the donors is striking. Six of the seven donors have been given the mandate to proceed with this approach and are advancing the development of policy and procedure accordingly. Currently, they are at slightly different points of progress. This is not to say that there is not any constraint.

9.1.3 This constraint is not embodied within the SAIs. Their role should not be underestimated. However, they do not challenge policy. Largely they measure the performance by the standards the donors set themselves. The fiduciary responsibility rests within the donor in the person of the accounting officer⁵⁹ and, of course, ultimately at the political level, with the minister. Aid is a risk business and it is they that must answer to parliament and the electorate. In doing so it is unlikely, given the complexity of issues, that there would be full understanding, should there be examples of waste or abuse.

9.1.4 However, these risks are not new, possibly just more apparent. Together with the new development thinking has arisen a heightened concern for accountability within the aid community. Paradoxically at the same time as apparently more liberal, less conditional and less obviously controlled disbursement is being seen as an inevitable consequence, the need for improved governance, control of corruption and the recipient governments accountability to their own electorate is becoming paramount. It is integral to the new paradigm. How is it to be realised?

9.1.5 It is beyond these TORs to answer that question, although some small contribution is attempted. The purpose of this study is to further the harmonisation of donors accountability requirements. There is a difficulty even in that because six of the

⁵⁷ This is not a suggestion that the WB take sole responsibility. It is likely that the WB would be seeking resources in the form of bi-lateral participants.

⁵⁸ With the exception of Germany, for the time being.

⁵⁹ Accounting officer: the accountable head of agency.

donors display remarkable flexibility (and variability) in their requirements. Hence budgetary support is disbursed in some countries with the worst record of financial management. At the same time decisions are made in more controlled environments not to pool at sector level, whilst perhaps disbursing to budget with minimalist accountability, despite the lessons of fungibility. It is something of these inconsistencies and paradoxes that has made the issue so intractable.

9.1.6 In this study the issue has been examined in terms of policy, systems and information. Most of the problems appear to lie in the latter category:

- (i) The donors have not completed the process of translating the will and policy position into guidance, tools and procedures.
- (ii) All face uncertainty about what is allowed by their own rules and what they may be allowed to “get away with”.
- (iii) There are change management issues. Not all staff necessarily understand (it is extraordinarily complex) and many may have doubts and or nervousness to take responsibility.
- (iv) The donor/embassy mind-set is still dominated by projects. Sector specialists are having to deal with issues beyond their experience. Macro-economists are having to learn to justify resource transfers on a wider range of criteria.
- (v) A large part of managing change is clear direction and firm management but the requirements here are more than just edict, clear procedure and some training. It is about hearts and minds. It is also about new analytical skill sets, for which some existing staff may not be equipped.
- (vi) There are no quick fixes. There appears to be no option but enhanced co-ordination but this has to be achieved over the “long-haul”. This will require the continuation for an indefinite period of a programme of internal reviews, studies, workshops and discussion at the various fora.

9.2 COMMON ACCOUNTABILITY REQUIREMENTS

9.2.1 In part the discussions during the visit phase of the study on core or minimum accountability/reporting requirements were an attempt to establish whether there were any immutable requirements. From this it is believed that there are no discernible minimum requirements on accountability, from which a common position could readily be written up. On the contrary there is every evidence of ad-hoc positions (country specific) and inconsistency from country to country and even within a country. As part of this study Ireland Aid and Norad have defined a minimum requirement. Whilst these would appear to be useful building blocks towards a common requirement both have their roots in financial accounting rather than broader measures or indicators.

9.2.2 Other donors have stressed their flexibility and, indeed, one suggested that common minimum standards may *not* be desirable. Another that there should be much firmer consensus in the following areas and that in designing these an approach should be adopted which permits as many countries as possible to participate, even if this does not meet some of the more ambitious ideas:

- commitment and disbursement mechanisms;
- reporting requirements and progress control arrangements;
- accounting arrangements.

9.2.3 This does not mean that fiduciary responsibility is taken any less seriously by those that do not advocate a core requirement but their preferred position is one of flexibility in order that all criteria can be weighed up and risk assessments made on a case by case basis. It is possible for example, that a common minimum standard would have prevented the Mozambique Macro-Fiscal MOU (7.2.2(v) above), from moving forward. It is also true that were a core requirement to be so minimalist it has to be questioned whether it would have any value at all.

9.2.4 This is not to say that a set of common or minimum requirements could not be arrived at, only that it would take considerable effort to construct. Whichever way it is looked at there has to be a common *position*, even if that is that donors agree to disagree on certain issues.

9.3 RECOMMENDATIONS

9.3.1 Donors need to further define their “bottom line” in terms of accountability. Better still, a new common and flexible position should be developed. This could include a minimum or core requirement, if it is agreed that donors want to adopt that approach but a decision needs to be made on whether this is desirable.

9.3.2 The paradox of the need for additional accountability at the SWAp level (as opposed to the budgetary level), needs to be resolved in order to bring clarity.

9.3.3 In order to be in a position to respond flexibly to the MTEF donors need to conduct further internal review (and possibly discussion with treasury) on their budget categorisations, which result in panic year-end spends and constraint on multi-year (firm) commitments.

9.3.4 Budgetary dialogue for both SWAps and budgetary support should place more emphasis on out-turn and trends in out-turn (over budget) over several years.

9.3.5 Issues of policy emphasis such as anti-corruption and democratisation need to be resolved. These might be addressed through the development of a code of conduct.

9.3.6 Donors should not place unrealistic measures of performance in the agreements with recipients as it is by these that their own performance and effectiveness will be measured (by the donor SAIs and beyond).

9.3.7 Headquarter support to embassies should be provided at critical junctures of appraisal and joint partner co-ordination discussions.

9.3.8 In framing agreements with recipient countries, donors and recipient governments should take account of the purpose and status (supremacy) of SAIs. This would include not placing unrealisable demands on the recipient SAI, particularly where they have not been consulted.

- 9.3.9 Whilst it has been concluded that the donor SAIs will not give the donors the comfort of “buy-in” to the new paradigm, nevertheless it is recommended that the dialogue with them should continue⁶⁰ both in terms of:
- Them being appraised of thinking and developments including the efforts the donors are making to address complex issues. In the event that donors, in the interests of harmonisation, perhaps have to give-up certain of their existing accountability requirements, that this is done in consultation;
 - Widening their scope of involvement in capacity building of recipient SAIs⁶¹.
- 9.3.10 The status and performance of recipient SAIs is moved up the development agenda (rather in the manner that revenue agencies have been previously). This would include measures of capacity building and institutional development (rather than just training). Such initiatives could continue to include the involvement of donor SAIs.
- 9.3.11 The INTOSAI standard is accepted by donors as the common standard for recipient SAIs (in so far as the standard on its own is meaningful and given that it may not be imposed). Reliance on recipient audit institutions should be considered more in terms of their independent status and professionalism rather than in terms promoting minimum acceptable (international) standards.
- 9.3.12 Enhanced efforts are made to increase civil society and private sector involvement. This is not necessarily meant in terms of greater stakeholder consultation or a role in co-ordination but in terms of measures towards greater government transparency and service expectation. A role for civil society could exist in furthering the independence of SAIs.
- 9.3.13 A donor code of conduct (guidelines) for the co-ordination necessary for the new paradigm should be worked up. These guidelines would be for both the appraisal and monitoring and evaluation stages (implementation) of the programme lifecycle.
- 9.3.14 Donors share assessment tools and other appraisal tools, agreeing a common approach and terminology.
- 9.3.15 The World Bank take the primary role in assessment of government budgeting and financial management capacity and benchmarking the need for improvement and measuring improvement over time. This would include, inter-alia the CFAA for the accounting side of the financial management equation. This should include an improved procurement capacity assessment (CPAR).
- 9.3.16 The UNDP PACT diagnostic tools (CONTACT) should be appraised and any future assessment tool design should absorb the lessons from this previous harmonisation initiative (although much of the donor material will now be out of date).
- 9.3.17 MOUs related to budgetary support, SWAps and recipient donor co-ordination meetings should avoid the language of contract.

⁶⁰ A view not shared by all SAIs as some will see participation as not being in line with their role.

⁶¹ Sweden (both Sida and the SAI) and the Netherlands SAI, are already involved in strengthening SAIs, in some cases in conjunction with the donor.

9.3.18 Donors re- examine why they use their chosen form of bilateral agreement (treaty/contract or EON).

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