

ASIAN DEVELOPMENT BANK

TAR: 36483-01

TECHNICAL ASSISTANCE

TO THE

FEDERATED STATES OF MICRONESIA

FOR

CAPACITY BUILDING IN PUBLIC SECTOR FINANCIAL MANAGEMENT

October 2002

CURRENCY EQUIVALENTS

The United States dollar is the currency in the Federated States of Micronesia.

ABBREVIATIONS

ADB	–	Asian Development Bank
BPS	–	Budget Preparation System
DFA	–	Department of Finance and Administration
FMIS	–	financial management information system
FSM	–	Federated States of Micronesia
TA	–	technical assistance
US	–	United States

NOTES

- (i) The fiscal year (FY) of the Government ends on 30 September. FY before a calendar year denotes the year in which the fiscal year ends, e.g., FY2002 begins on 1 October 2001 and ends on 30 September 2002.
- (ii) In this report, "\$" refers to US dollars.

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I. INTRODUCTION

1. In 1995, the Government of the Federated States of Micronesia (FSM) initiated a reform program aimed at strengthening the economy. The Asian Development Bank (ADB), through its Public Sector Reform Program loan and associated technical assistance (TA)¹ has been supporting the reform activities. One element of the reform program is the introduction of a performance-based budgeting system to enhance financial controls and improve public resource management. This initiative has been supported by a number of TAs² since 1998 to improve the management of public resources through development and implementation of a performance-based public resource management system. Activities undertaken have achieved the following: (i) performance-based budgeting was introduced in the FSM's national and four state governments; (ii) new budget and accounting procedures were implemented; (iii) training was held to improve capacity in strategic planning and understanding of performance-based concepts and terms; (iii) an improved budget preparation system (BPS) and a detailed budget manual were introduced.

2. The first phase of TA FSM-3765 involved a review of the budgeting, accounting, and management reporting systems currently in use in the five governments. The review indicated some systems and capacity deficiencies that have limited the efficiency and effectiveness of the performance-based budget management reforms (para. 7). The 2002 Country Programming Mission agreed with the FSM governments that the adoption of a uniform financial management information system (FMIS) by all governments will improve efficiency and effectiveness, and enhance accountability and transparency of government operations. Discussions between ADB, the FSM government, and the United States (US) Department of Interior resulted in an understanding that the TA should have two components: (i) the acquisition of hardware and software and installation of an integrated FMIS in all five governments, to be funded by the US Government; and (ii) a comprehensive training program for FSM officials in accounting, finance, and management principles and systems, with ADB assistance. Funding from the US Government has been confirmed in discussions with the FSM and the US Department of Interior officials.

3. This TA³ supports comprehensive capacity building in accounting, budgeting, and information technology with specific focus on performance-based public resource management. The TA will reinforce performance-based budgeting reforms supported by ADB since 1998 (footnote 2).

II. ISSUES

4. The objective of introducing performance-based public resource management is to improve the quality and effectiveness of resource management. Earlier work under TA 2983 and TA 3431 focused mainly on designing performance-based budgeting software and training on how to use the BPS to prepare the annual budgets.

¹ ADB. 1997. *Report and Recommendations of the President to the Board of Directors on a Proposed Loan to the Federated States of Micronesia for the Public Sector Reform Program*. Manila; ADB. 1995. *Technical Assistance to the Federated States of Micronesia for Policy Advisory Team for Economic Management*. Manila.

² ADB. 1998. *Technical Assistance to the Federated States of Micronesia for Performance-Based Public Resource Management*. Manila; ADB. 2001. *Technical Assistance to the Federated States of Micronesia for the Implementation of Performance-Based Budget Management*. Manila.

³ The TA first appeared in the *ADB Business Opportunities* (internet version) on 3 September 2002.

5. In the deliberation on the 2002 budget in the 12th session of the FSM National Congress, the performance-based budgeting approach was discussed extensively by the Public Accounts Committee. The committee's report, while indicating continued frustration with the budget process and output, confirmed its commitment to the concept and the need for performance-oriented budgeting and reporting systems. The committee suggested simplification of the existing performance budget format and content to focus the budget on priority items and to improve ease of understanding by Congress. Understanding and support for the performance-based public resource management was expected to grow once the executive branches of all five governments improved the quality and user-friendliness of the documents, and demonstrated its usefulness in the management of government operations.

6. The usefulness of a public sector FMIS depends, in large part, on its ability to link the budget preparation and financial reporting modules. The first phase of TA 3765, a review of the existing systems (BPS, FMIS, and performance reporting) in the five governments, noted a number of deficiencies: (i) three FMISs of varying quality are in use; (ii) budget preparation is supported by a BPS that is a stand-alone system with no linkages to accounting or management reporting systems; (iii) the existing FMISs (except one) use old technology and hence suffer from inadequate supplier support; (iv) in-house technical expertise for BPS and FMIS is inadequate; (v) poor understanding of the concepts and requirements of the performance-based management by staff and decision makers; and (vi) lack of capacity and resources to adequately support the effective use by decision makers of available information.

7. The key recommendations arising from the first phase of TA 3765 are (i) the acquisition of a new FMIS that would support all functions needed to prepare annual budgets, properly account for actual expenditure, and prepare reports for compliance and performance monitoring purposes; and (ii) a comprehensive and sustainable training program for staff to successfully implement and maintain the new FMIS. The training should include information technology subjects that are needed to develop and maintain the new computerized FMIS, and basic concepts and principles of budgeting, accounting, and management in the FSM public sector context.

8. A prerequisite to successful implementation of any new system is that staff involved in implementation and maintenance have the required skills and capabilities for the tasks required and to maintain the system. In addition, those receiving information produced by the system must be able to use the information for management planning and control purposes. The TA is an essential component of the agreement with the US Department of Interior to work toward a streamlined computer system in offices of all five governments, a system that will be supported by a continuing, self-sustaining training program in financial management and modern concepts of public sector management.

III. THE TECHNICAL ASSISTANCE

9. The TA aims to further develop sound financial management and planning capability in all five FSM governments. Successful installation of new software requires effective change management as well as commitment of all involved. Senior officials confirm the commitment and readiness of the governments to promote a culture of performance-oriented management in public service operations. The support of the US Government will complement the assistance provided by ADB and reduce the need for prolonged TA in this area.

A. Purpose and Output

10. The TA will finance consulting services to provide on-the-job training to staff engaged in the pilot implementation of a new FMIS in the Department of Finance and Administration (DFA) of the FSM's national Government. The consultants will also be the focal point for advice on any changes to users' specifications during the FMIS implementation. The TA will also produce training materials in (i) financial management, business planning, and performance-oriented management; and (ii) basic information technology technical and user support. Training will be geared to the specific needs of FSM governments to support the performance-based budgeting and management reporting systems associated with the new uniform FMIS. The training will likely be recognized by the College of Micronesia,⁴ which will provide credits for staff wishing to acquire formal qualifications in accounting or business management.

11. Given the serious shortage of accountants in the FSM, the training supported by the TA will provide a pool of students who could complete the formal accountancy qualification programs offered by the College of Micronesia, and thereby reduce dependence on foreign accountants.

B. Methodology and Key Activities

12. The TA will be a collaboration between consultants engaged under this TA and staff of the College of Micronesia's Business Division. The consultants, in collaboration with the relevant teaching staff of the college, will develop the content and delivery of the following training courses:

- (i) **Information Technology.** (a) development of users' skills with computer systems, with specific reference to the new software to be acquired, including some basic computer knowledge; and (b) technical training for information technology (basic operating systems, and database maintenance);
- (ii) **Public Sector Management Principles.** general management concepts and principles with specific reference to the management processes adopted by FSM public sector (e.g. the public sector budgeting processes, including the role and responsibility of stakeholders [Congress and executive agencies], performance budgeting concepts and practices, business planning by departments, etc.); and
- (iii) **Accounting and Financial Management in the Public Sector.** basic accounting concepts and principles, public sector accounting terminology, accounting and reporting requirements of FSM governments based on the new FMIS, (including two courses in this area, the first for staff who will be working in finance/accounting positions and therefore will need more technical accounting/budgeting training), and the second for nonfinance staff who require only general knowledge of government budgeting and financial requirements, basic principles of accounting, how the reports are put together, and how the information can be used for management purposes.

⁴ The Business Division of the College of Micronesia offers a 2 year degree in Accounting-Finance, a post secondary qualification. Preliminary discussions between ADB staff, the College, and the DFA indicated strong support for the proposed collaboration to ensure ongoing training to support the Governments' needs for public sector accountants and information technology professionals. It is intended that the DFA will contribute toward the cost of the College's involvement in this project.

13. The desired output of the TA will be the smooth implementation of the new FMIS based on effective use of training materials covering the above subjects. The consultants and the college's teaching staff will collaborate in the delivery of training to the initial groups of staff who will be involved in implementing the new FMIS. Subsequently, the college will liaise with the five governments to roll out the courses to other staff on a "user pays" principle in its state campuses. The college, in conjunction with the five departments of finance and administration, will likely offer the courses to staff on an ongoing basis to meet the emerging needs of the governments.

C. Cost and Financing

14. The total cost of the TA is estimated at \$460,000. ADB will finance \$360,000 of the costs of international consultants (covering \$350,000 of the foreign costs and \$10,000 of the local costs). The Government will cover local costs, estimated to be \$100,000, relating to expenses of local counterparts, including fees to the College of Micronesia for its involvement in developing the courses, and costs relating to workshops and printing of training materials. The TA will be financed on a grant basis by ADB's TA funding program. Detailed cost estimates are in Appendix 2.

D. Implementation Arrangements

15. The DFA will be the Executing Agency. A steering committee will be established consisting of one representative from DFA, two from state departments of finance, and one from a line agency of the national Government. The deputy secretary, DFA will chair the steering committee and will be assisted by the team leader and/or local counterpart engaged under the TA.

16. A team of international consultants will be engaged by ADB and will provide approximately 15 person-months of consulting services on an intermittent basis. The team will comprise (i) a team leader with extensive experience in public sector accounting and training, in particular performance and output-based budgeting and accounting (9 person-months); (ii) an information systems training specialist with experience in accounting applications used in the public sector (3 person-months); and (iii) a training specialist with experience in public sector financial management (3 person-months). The consultants will be individually selected and engaged in accordance with ADB's *Guidelines on the Use of Consultants*. The national government will engage the College of Micronesia to collaborate in preparing the training materials with a view to taking over training activities at the completion of the TA. The consultants will need to work cooperatively with the consultants from the ADB-financed Economic Reform and Capacity Building Project and other externally-assisted projects, in particular the FMIS replacement project to be funded by the US Department of Interior. The outline terms of reference for the consultants are in Appendix 3.

17. The TA will be implemented over a period of 17 months, from February 2003 to June 2004. The team leader, to be assisted by a local counterpart to be provided by DFA, will be responsible for coordinating the work of team members. The consultants will contribute to the progress and final reports to be prepared by the team leader. Each consultant, however, will prepare his or her final report on specific achievements and lessons learned under the TA, covering his or her particular area of expertise/responsibility.

IV. THE PRESIDENT'S DECISION

18. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$360,000 on a grant basis to the Government of the Federated States of Micronesia for Capacity Building in Public Sector Financial Management, and hereby reports this action to the Board.

TECHNICAL ASSISTANCE FRAMEWORK

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Goal Improved management of public resources.</p>	<p>Measurable changes and trends in public sector expenditure in priority areas.</p> <p>Passage of the 1999 draft financial management legislation by Congress.</p> <p>Consolidated report on income and expenditure of all the Federated States of Micronesia (FSM) governments.</p>	<p>Published financial statements over the years subsequent to implementation.</p> <p>Performance budget for Congress' approval and within year financial reports.</p> <p>Management reports prepared on an exception basis, i.e., variances from performance-based budgets and plans.</p>	
<p>Purpose Enhanced capacity of public servants to maintain the performance-based financial management information system (FMIS), and to support users of information and reports generated by the FMIS.</p>	<p>Timely, simplified, and user-friendly performance budgets.</p> <p>Reports to Congress, President, and secretaries of departments on same basis as budget, with meaningful explanation provided for variances from budget and plans.</p> <p>FMIS working smoothly by end of FY2004 and providing regular quality (no system-generated errors) reports and ad hoc information as requested by users.</p>	<p>Format and content of annual budgets and regular reports to Congress and the President.</p> <p>Consultants' and steering committee's reports on progress of implementation.</p>	<p>Unsuccessful implementation of the FMIS, which is to be supported by the United States (US) government.</p> <p>Delay in FMIS implementation.</p>

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
	Technical system and user support provided by staff.		
<p>Outputs</p> <p>1. Training materials on</p> <ul style="list-style-type: none"> (i) Information technology technical support generally and knowledge specific to the FMIS software selected for implementation in the FSM. (ii) General management concepts and principles with specific reference to the management process in the FSM public sector. (iii) Budgeting and accounting in the FSM public sector, for finance staff. (iv) Budgeting and accounting in the FSM public sector, for nonfinance managers. <p>2. Delivery of the training to the initial groups of staff, estimated at 150.</p>		<p>Comments from steering committee members on the relevance and appropriateness of draft materials.</p> <p>Feedback from course participants.</p>	

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Activities</p> <ol style="list-style-type: none"> 1. Document public sector's management process. 2. Document FSM's budgeting and accounting processes and procedures. 3. Determine information technology support requirements of the selected software for the new FMIS. 4. Draft training materials for the courses. Circulate for comment of steering committee members. 5. Undertake pilot training sessions for staff directly involved in the new FMIS implementation. 6. Prepare timetable for training of other staff. 	<p>Meeting timetable for preparation of materials.</p>	<p>Steering committee's reports.</p> <p>Availability of local counterparts to undertake training as planned.</p>	<p>Full commitment by five governments.</p>
<p>Inputs</p> <p>Recruit international consultants for public sector accounting and information technology.</p> <p>Liaise with College of Micronesia to ensure their participation in the TA.</p> <p>Financial resources provided by</p>			

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
the national government and the Asian Development Bank.			

COST ESTIMATES AND FINANCING PLAN
(\$'000)

Item	Foreign Exchange	Local Currency	Total Cost
A. Asian Development Bank Financing^a			
1. Consultants			
a. Remuneration and Per Diem of International Consultants	280.0	0.0	280.0
b. International and Local Travel	35.0	5.0	40.0
c. Reports and Communications	10.0	5.0	15.0
2. Contingencies	25.0	0.0	25.0
Subtotal (A)	350.0	10.0	360.0
B. Government Financing			
1. Consultants			
a. Remuneration and Per Diem of Domestic Consultants	0.0	50.0	50.0
b. Reports and Communications	0.0	10.0	10.0
2. Training, Seminars, and Conferences	0.0	15.0	15.0
3. Miscellaneous Administration and Support Costs	0.0	10.0	10.0
4. Office Accommodation and Transport	0.0	15.0	15.0
Subtotal (B)	0.0	100.0	100.0
Total	350.0	110.0	460.0

Source: Asian Development Bank estimates.

^a ADB TA Funding Program

OUTLINE TERMS OF REFERENCE FOR CONSULTANTS

A. Scope and Work Program

1. The key purpose of the technical assistance (TA) is to enhance the capacity of the Federated States of Micronesia (FSM) public sector to support the implementation of performance-based public finance management without reliance on foreign experts. The TA aims to institutionalize an acceptable level of support in financial management and information technology technical knowledge to ensure that staff and users understand the purpose and requirements of performance-based management and the linkage with the new FMI system as they are implemented by the five governments.

2. The consultants engaged under the TA will provide training of local staff in the requirements of performance-based public finance management as applied in the FSM and as incorporated into the new financial management information system (FMIS). The FMIS will support the budgeting, accounting, and performance monitoring activities under the performance-oriented management system. The learning experience and lessons arising out of this process will be used to develop training materials for the training program for other staff in line agencies and new staff.

B. Specific Terms of Reference

1. **Public Sector Financial Management Specialist, Team Leader** (9 person-months)

3. The team leader should have had extensive experience in public sector accounting and budgeting, especially under a performance-based system. The person is expected to provide the technical leadership in applying the performance-based management concepts and practices to suit FSM circumstances, and will do the following:

- (i) with assistance from the training specialist and staff of the College of Micronesia, prepare a training program and timetable to ensure a successful implementation of the new FMIS;
- (ii) liaise with the FMIS project leader to ensure the training program supports the piloting and full implementation of the FMIS;
- (iii) provide on-the-job training for and advice to members of the FMIS implementation teams, in particular performance-based concepts and practices appropriate to FSM circumstances;
- (iv) oversee the technical content of the training materials in accounting, budgeting and performance monitoring as applied in the FSM, with assistance from the training specialist and College of Micronesia staff;
- (v) oversee and participate in, as appropriate, the initial workshops on the new FMIS to staff of the states' implementing agencies;
- (vi) supervise the implementation of the training program to other sites in the national and four state governments, with assistance from the local counterpart; and

- (vii) assist through the local counterpart, the FMIS steering committee as required with respect to the training program.

4. The team leader is responsible for preparing (i) an inception report setting out the training plan during the implementation of the FMIS; (ii) a progress report at the end of the pilot implementation period giving lessons learned with respect to training; (iii) progress reports to the implementation steering committee and Asian Development Bank; and (iv) a final report on the results of the training program at the end of the FMIS installation, and recommendations on future training activities (through the College of Micronesia) to ensure new staff in the national and state governments have the knowledge necessary to support the performance-based resource management as implemented in the FSM.

2. Information Technology Training Specialist (3 person-months) and Financial Management Training Specialist (3 person-months)

5. The training specialists should have a proven record of successful preparation of training materials and delivery of training workshops in the field of expertise for which they are chosen:

- (i) Information technology training will apply specifically to the software selected by the government to support the performance-based accounting and budgeting systems. The specialist will need to work closely with the software supplier in developing training materials and delivering the workshops. This training focuses on users rather than technical support staff, who will be trained by the software supplier.
- (ii) Public sector financial management training will be for accounting staff and nonfinance managers.

6. Each specialist will work closely with, and support the team leader to ensure successful training during FMIS implementation and the transfer of skills to local counterparts, including College of Micronesia staff, to ensure continued training in the future.

7. Each specialist will prepare reports as required by the team leader for input into reports to the Asian Development Bank and the steering committee.