LINKED DOCUMENT 4: FIDUCIARY ASSESSMENT

Overview

1. Results-based lending (RBL) is an innovative form of financing developed by the Asian Development Bank (ADB) and other development partner organizations in response to changes in the developing country context. In recent years, development partners have become increasingly aware that only a small fraction of development finance consists of official development assistance (ODA). Organisation for Economic Co-operation and Development (OECD) data\(^1\) show that non-ODA flows (foreign direct investment, commercial bonds, philanthropy, other official developmental flows, officially-supported export credits, other private flows at market terms, private grants and remittances) made up 82% of total flows to developing countries in 2015, with 86 developing countries having ratings from at least one of the three largest international rating agencies by 2007.\(^2\) In 2015, official ODA was only 18% of the total, the same proportion as in 2000. To leverage this small contribution to overall financing, ADB and other traditional development partners are shifting their orientation toward pilot-testing, innovation, and learning.

2. An important part of this new approach to development assistance is a commitment to use systems for aid administration. Program systems include, for example, using national budget preparation, execution, inter-governmental transfer, and audit processes, including putting projects on-budget, timed according to the government’s fiscal calendar, and using national competitive bidding procedures. Other program systems may be used including civil service personnel rules, and systems for safeguards, monitoring, and evaluation.

3. In the past, development partners often found it necessary to bypass program systems due to perceived risks. However, in recent years, while acknowledging the risks, they have seen many benefits in working within program systems. The expected benefits are reductions in implementation delays and transaction costs, improvements in country ownership, and stronger institutional capabilities for service delivery. This is in line with global declarations of aid effectiveness.\(^3\) Examples of using program systems for ADB and other external funding include reporting in developing member country (DMC) budget documentation, managing disbursements through DMC treasury systems, accounting, and reporting using DMC’s own classification and financial reporting systems, auditing by DMC system without any additional special requirements, and managing procurement with DMC procedures. A World Bank evaluation found that for projects approved after the Bank adopted its Governance and Anticorruption Policy, which prioritized the use of country systems, 41% of projects in countries with weaker institutional capacities used at least some of these systems, compared to 27% of projects before the policy was adopted.\(^4\)

4. ADB has moved in recent years to use country systems as they become more robust, and as DMCs increasingly prefer to use these systems. This may start as a hybrid approach using some systems, and then adding more as they improve. Reportedly in 2010, 94% of ADB-financed operations used DMC transaction costs, improvements in country ownership, and stronger institutional capabilities for service delivery. This is in line with global declarations of aid effectiveness.\(^3\) Examples of using program systems for ADB and other external funding include reporting in developing member country (DMC) budget documentation, managing disbursements through DMC treasury systems, accounting, and reporting using DMC’s own classification and financial reporting systems, auditing by DMC system without any additional special requirements, and managing procurement with DMC procedures. A World Bank evaluation found that for projects approved after the Bank adopted its Governance and Anticorruption Policy, which prioritized the use of country systems, 41% of projects in countries with weaker institutional capacities used at least some of these systems, compared to 27% of projects before the policy was adopted.\(^4\)

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financial management systems such as accounting, auditing, and financial reporting, compared with a Paris Declaration target of 78%.  

5. With RBL, ADB supports a small part of a larger government program, implemented using the country's own financial management and procurement systems. The RBL approach is to use program systems applying to specific programs, which may be higher quality than those for other programs. Benefits include an opportunity for ADB to gain in-depth knowledge on the program systems supporting a sector, and for DMCs to deepen their own understanding about how to improve their own systems, and the impact of their programs in the medium to long term, so that using program systems becomes the norm. This is part of a wider effort by ADB to use country systems.  

6. This comparative synthesis looks at the 12 RBL operations approved by the end of 2016 and assesses the quality of expenditure frameworks and fiduciary assessments, and the appropriateness of the capacity development and other measures to strengthen systems and practices. Some comparisons with norms and practices at the World Bank will be made, along with recommendations on what can be done to strengthen these aspects in RBL programs.  

7. The first section of the paper presents the analytical underpinnings supporting the RBL approach and the conditions under which RBL programs are likely to be the preferred modality. The second section looks at the quality of expenditure frameworks in the 12 RBL operations, based on desk reviews and field missions. Questions to be addressed include the following. Was there an adequate definition of the RBL's program's expenditure framework, including the scope and boundary vis-a-vis the broader government program? Is ADB's value addition clearly articulated? Is it likely that results can be achieved within the program's resource envelope? Is the financing plan predictable, and likely to be sustained? Are the proposed measures to strengthen the expenditure framework appropriate to address risks and shortcomings?  

8. The third section looks at the quality of fiduciary assessments and proposed measures to mitigate risks and other shortcomings. Questions to be addressed include the following. Were the fiduciary assessments of overall and program financial management, procurement, and fraud and corruption systems adequate to ensure that program funds will be used for intended purposes? Are the proposed measures to strengthen program fiduciary systems and governance appropriate to address risks and shortcomings? The final section presents a summary of findings, conclusions, and recommendations.  

Analytical Underpinnings  

9. RBL is a learning-by-doing approach that enhances ADB's results orientation. It takes a principle-based rather than rule-based approach intended to improve the program systems for an entire DMC program. RBL complements other ADB instruments, including investment lending, policy-based lending (PBL) and the multitranche financing facility. PBL uses country systems and disburses based on the adoption of critical, ambitious policy reforms. Investment lending uses a combination of country and ADB systems for financial control and procurement and disburses based on proof of authorized expenditures. The multitranche financing facility uses a combination of ADB and country systems and disburses in multiple tranches to finance different components of an investment program. The intention is that a combination of these lending modalities will best deliver DMC's priorities around results while scaling up country and program systems whenever possible.

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10. There are many assumptions embedded in the RBL analytical framework that need to be unpacked. First is the presumption that working with program systems will help strengthen them. There is evidence that this can be the case. For example, a study of general budget support found that in five of the seven countries with established track records, channeling aid through country systems had strengthened budget processes, including comprehensiveness and transparency. There are at least three reasons for this: (i) development partners and sector ministries are more likely to put financing on-budget to comply with program agreements; (ii) development partners pay closer attention to the quality of a country’s fiduciary controls and systems to protect their own resources passing through these systems; and (iii) by adopting the government standard, development partners can avoid multiple procedures and reduce transaction costs. In addition, an evaluation of World Bank support to public sector reform found that sustaining efforts to reduce corruption have better prospects when they emphasize: (i) building country systems that reduce the opportunities for the costliest forms of corruption and (ii) stimulating citizen demand for more efficient and less corrupt service delivery by making information public.

11. At the same time, there are concerns over the risks of using program systems, including fiduciary mismanagement, diversion to lower priority developmental areas, delays, and damage to donor's reputations should these risks materialize. For example, research on World-Bank-funded education projects in Malaysia found that when the government implemented them, they suffered from unexpected cost increases, delays, sole source contracts, and other shortcomings resulting in part from the lack of qualified staff, and heightening the risk of fraud and corruption. When the World Bank directly implemented similar projects using project implementation units, procurement and financial management were carried out to a higher standard, leading to fewer delays, reduced costs, and higher quality results. According to a World Bank survey, staff felt that there was a higher risk of complaints for fraud and corruption on projects using country systems, so they added additional World Bank supervision and transactional reviews. There may also be a risk to the donor who uses country systems first and incurs a short-term cost, which ultimately provides a public good for all donors.

12. Drawing on these and other research findings, this background paper looks at the evidence of the 12 ADB RBL operations approved through the end of 2016 to assess whether the benefits of working through fiduciary and procurement program systems are likely to outweigh the risks of doing so.

13. A second assumption embedded in the analytical framework is that the costs of achieving the intended results can be and are being accurately estimated up front. Accurate costing is important for many reasons: (i) accurate costs are needed to prepare and review budgets for the overall government program, and for the specific portion being supported by the RBL; (ii) costs are needed to measure performance in terms of cost per unit of output, to help determine if the costs incurred in achieving the objectives were reasonable and in line both with the benefits produced, and with recognized norms; (iii) contract planning needs to consider market structure and supply chains, contract design and methodology, and to ensure adequate costing and budgeting; (iv) a good measure of service cost is needed to measure the cost of policy choices, and to take into account in setting prices for social services; (v) market testing may be appropriate, and if so needs cost comparisons among alternatives; and (vi) there can be other types of costs incurred when corruption takes place.

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http://etheses.bham.ac.uk/1119/

https://openknowledge.worldbank.org/handle/10986/16674

14. Diverted costs can lead officials to intentionally design programs to facilitate corruption. Failure costs occur when a program uses its resources without achieving the intended results. Total costs comprise direct costs such as labor and raw materials that can be assigned to producing particular outputs, and indirect costs or overhead shared among several outputs. For example, one may start by identifying activities, then assigning costs to the activities based on both direct tracing and surveys, then identifying the outputs produced by the activities, and finally assigning activity costs to the outputs. Allocating overhead to activity costs is particularly difficult, and may be estimated based on a ratio to a direct cost such as labor. Overhead costs include fiduciary costs necessary to prevent and detect corruption, and the efficiency cost caused by the interference of effective design or implementation by fiduciary controls. Some governments go further and account for the full costs of capital assets as part of overhead.14

15. Assessments of the cost of producing outputs and outcomes in RBL operations will be based on many questions. Were standard unit costs used based on country experience (e.g., for deliverables such as vaccinations given, roads built)? How were costs estimated for softer targets, such as institutional strengthening involving behavioral changes that would seem to be difficult to cost? The premise here is that, if the cost is overestimated, there would be a surplus that could be stolen or used for bribes or just wasted. If costs are underestimated, there is a risk that once true costs are understood, disbursement-linked indicators (DLIs) might no longer make economic sense. How are actual costs tracked, reviewed, and reported during program implementation?

16. A third assumption is that it is possible to carry out a fiduciary assessment and to come to a reliable, clearly formulated conclusion. In cases where fiduciary weaknesses are apparent, capacity development and risk mitigation actions are identified. The idea is to bring sound fiduciary principles to the DMC’s own financial management, procurement and anticorruption processes, not to adopt ADB rules and procedures. ADB will support the DMC during program implementation in these areas, and assess progress during supervision through monitoring of loan agreement conditions, DLIs, program action plans (PAPs), and other risk mitigating measures as appropriate.

17. A further challenge underlying the assumption behind system strengthening is the distinction between strengthening formal and functional aspects. There are some areas where progress can be achieved through adopting a new law, regulation, or technical tool, or focusing on no more than a few agencies, or at an early stage in the budget cycle. For example, public expenditure and financial accountability (PEFA) indicator PI-4.1, “government budget and accounts classification is consistent with international standards,” is of this type. These aspects are the most likely to improve or maintain a good score in a PEFA assessment, and can be termed formal public financial management (PFM) or procurement features. On the other hand, functional features are less likely to improve: that is when progress requires implementing a new law or regulation in letter and in spirit, or coordinating the work of many agencies, or working downstream in the budget cycle. For example, PEFA indicator PI-7, “transparency and timeliness of transfers from central government to subnational governments with direct financial relationships to it ... and whether subnational governments receive information on their allocations in time to facilitate budget planning,” is of this type. The difference is most pronounced for features where progress can be achieved working with the Ministry of Finance and/or just a few other agencies, in comparison with PFM features where many agencies are involved. Likewise, functional

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14 Schiavo Campo and Tommassi, footnote 13, p. 249.
features are more likely to worsen or maintain a low score than formal features.\textsuperscript{15} Measures proposed to
strengthen program systems must ensure a good balance of formal and functional. If the measures are
only formal, there could be good laws and regulations in place that aren’t implemented as intended, so
they would not lead to an adequate fiduciary environment. Care must be taken also to ensure that more
challenging functional measures are adopted successfully.

Quality of Expenditure Frameworks

18. This section addresses many questions based on desk reviews of 12 RBL programs, and field
missions to nine of them. First: was there an adequate definition of the RBL’s program’s expenditure
framework, including the scope and boundary vis-a-vis the broader government program? In most of the
operations, the scope and boundary were clear, and the costing methodology explained. For example, in
Supporting National Urban Health Mission in India, cost estimates are based on norms and unit rates for
different program components and subcomponents, including program management, urban community
health center, urban primary health clinics, and medicines. There were also norms used for health workers
per population, social health activist per slum or vulnerable households, and training modules. In other
cases, costs were estimated with support from ADB project preparation technical assistance consultants.

19. Questions can arise when the expenditure framework covers a long-time period and when there
is uncertainty about government budget resources for the program. For example, the School Seismic
Safety Improvement Program in Armenia is a 5-year time slice of a 15-year program. The initial 5-year
program covers 46 schools, and the latter an additional 377 schools. No information is provided about
any funding lined up for the longer program, which is a concern, and the costing of the longer program
seems inconsistent with that of the shorter one. Due to fiscal constraints the government has agreed
with the International Monetary Fund to reduce fiscal expenditures, which includes planned expenditures
on the RBL program. In this instance, the RBL modality is proving to be a disadvantage since ADB can
only reimburse actual budget expenditures on the program when DLIs are achieved.

20. Another issue came up with Public–Private Partnerships Demonstration Program to Transform
Delivery of Elderly Care Services in Yichang, Hubei in the PRC. Cost estimates assume fiscal and efficiency
gains from will use a PPP arrangement. One aspect not discussed is whether “private” PPP providers can
be state-owned companies. In its PPP regulations, the PRC defines a nongovernment partner not as
“private capital,” but as “social capital” which can include state-run firms. One study found that, among
implemented demonstration projects selected by the government to show how PPPs should work, about
55% of the social partners are state-owned enterprises. A larger project database of PPPs cited by Bank
of America found that state companies were taking up 74% of the projects by value. Private investors
have been reluctant to join PPPs because of low returns, failed projects, and suspicion of government.
This is a problem because, while PPPs relieve financing pressure for Yichang and other local governments,
with state-owned enterprise partners the financing risk and debt burden may just be shifted to another
part of the state, and not picked up by the private sector. Further, the efficiency gains expected by private
sector management might not be realized if state owned firms are the PPP partners.\textsuperscript{16}

21. A second question is whether ADB’s value addition is clearly articulated. For many of the RBL
programs, ADB had previous experience in the sector, providing help in costing, and experience in
managing fiduciary risk. For example, in the case of Electricity Grid Strengthening—Sumatra, ADB and
the implementing agency, Perusahaan Listrik Negara (PLN), produced projected costs that are based in
part on ADB’s experience with the Power Transmission Improvement Sector Project in Indonesia,
implemented during 2002–2014. Prior experience can also be helpful in estimating future operation and
maintenance (O&M) costs. However, the Indonesia RBL does not distinguish the program boundary from

\url{https://pefa.org/content/pefa-monitoring-report-2010-repeat-assessments}

the broader government program, although the RBL is intended to support the distribution network, not the entire transmission and distribution system in Sumatra. Sri Lanka’s Education Sector Development Program does not delimit the RBL program boundary either but given the broad nature of RBL support the value addition of sector support to the broader government program is more plausible.

22. In the case of the Sustainable Transport Infrastructure Improvement Program in Solomon Islands, a different issue arose: even though maintenance of transport infrastructure is a priority issue, the government prefers to use ADB funds for investment, i.e., repair and rehabilitation, particularly for the East Guadalcanal road linking to the palm oil industry, since this will yield direct economic benefits that can contribute to loan repayments. The government has suspended borrowing for maintenance expenditures as part of its debt management strategy. Since the ADB contribution is less than the amount required for rehabilitation and repair, limiting ADB funding to investment finance is notionally achievable. The RBL allows the government to have it both ways: DLI1 disburses 17% of the total based on acceptable maintenance, but once the government gets the money, it is free to use it for eligible investment expenses under the program.

23. The Senior High School Support Program in the Philippines brings up another aspect of value addition. The Department of Finance informed the IED mission that RBL financing goes to the Treasury and is not provided as incremental financing to the Department of Education. This raises the question: What is the incentive for Department of Education to take on the additional burden of implementing and monitoring the RBL if they are not receiving additional funds to do so? The Department of Education told the evaluation team that the RBL support helped to protect its budget against the risk of cuts when the government changed. The department also said that ADB’s cofinancing of the government budget helped to ensure that the voucher program was fully funded and that other expenditures on classroom construction and education quality were not reduced.

24. Value addition is also evident in the shift from grants based on unit costs to performance- and needs-based grants. For example, Nepal’s Supporting School Sector Development Program includes the replacement of unit-based grants by needs-based grants for schools since their O&M needs may be quite different. This is possible because the Education Review Office undertakes a biannual survey which is being extended from student performance to school facilities. In another example, Sri Lanka’s Skills Sector Enhancement Program piloted performance-based contracting of private training providers to deliver training and job placement services. In an iterative process, the ministry experimented with different contractual conditions until they came up with something that all sides could accept. In this area, the RBL has encouraged a spirit of enquiry, a willingness to learn, openness to trying new approaches and, ultimately, a greater sense of ownership of the progress achieved.

25. One can imagine going a step further and using results-based funding for prizes in open competitions. There is a long history of this in the public sector for supporting technological innovation, going back at least to 1714 when the British Parliament offered the Longitude Prize for advancement in the measurement of longitude. The USA Defense Advanced Research Projects Agency prize was offered for the first autonomous vehicle to complete a 150-mile course in California, and was won by Google in 2010. Future RBL programs could also offer prizes funded through DLIs to achieve highly ambitious results for public goods and services where it wasn’t clear from the outset who could accomplish a difficult feat, or how they might do it. 17

26. The third question is whether the financing plan is predictable, and likely to be sustained. Again, in most cases, the RBL financing plans seemed to be sustainable. For example, in the case of Pakistan’s Access to Clean Energy Investment Program, mini-hydropower (MHP) schemes under two megawatts will be handed over to local communities for O&M. MHPs have a tariff regime with three parts—(i) a base

charge to cover the cost of the operator who will be hired by the communities and trained by the program; (ii) normal O&M expenses; and (iii) insurance against catastrophic damage where the entire unit needs to be replaced, managed by Pakhtunkhwa Energy Development Organization. The 200 or so MHPs that have been installed by nongovernment organizations in the northern districts are maintained by local communities who are used to paying the first two parts of this tariff, which is kept in a bank account managed by the community organization. The third part is new and will be more challenging to collect.

27. Another factor is that funding may be more predictable in the targeted sector than in the government as a whole. For example, in the case of the Supporting School Sector Development Program in Nepal, the latest PEFA found high variance between sectoral allocations and sectoral expenditures overall, averaging 11% over a 3-year period, but the variance in education averaged only 3% over the same period. Assuming the pattern continues, one can assume there will be reliable links between budget and expenditure for the program.

28. However, in some countries that have made budget allocations to support the program, there is still a risk of a failure of political incentives to stick to these allocations. The need to maintain patronage networks could be stronger than the incentive to stick to agreed priority allocations. For example, in the Solomon Islands, projected cash flows show that the funds will be sufficient throughout the 5-year program period with a positive cash inflow at the end of the program. However, the evaluation mission was told that the government is facing challenges in meeting its financing commitment. The annual government contribution is intended to finance all maintenance costs, and enforced by differently formulated DLIs from ADB and Australia’s Department of Foreign Assistance and Trade (DFAT). For 2016, the target for ADB’s DL13 of releasing SI$41 million was met. However, DFAT’s target of releasing SI$50 million was not met, meaning that the AS1 million performance-linked grant tied to this target was not released and was canceled. The evaluation mission was told that Ministry of Finance and Treasury had authorized the release to meet the DFAT target, but that other interests prevailed that decided to the use funds elsewhere. The evaluation mission was informed that the funds were reallocated to “shipping grants,” and “constituency grants,” which are politically motivated funds not closely monitored.

29. Another issue concerns the adequacy of funding outside the RBL program. For example, the evaluation mission was told that the Sri Lanka’s Education Sector Development Program expenditure estimates for 2013-2017 had already been exceeded as of 2016, with a drastic increase in capital expenditure between 2014–2015. However, this increased spending is not necessarily leading to improved learning outcomes, due to the lack of qualified teachers and other issues. To date, DL1 on increased O-level results has been exceeded, while DL2 on increased A-level results has not been achieved. Staff from the Ministry of Education and the Ministry of National Policies and Economic Affairs explained to the evaluation mission that it is difficult to recruit and retain teachers, particularly in areas such as science and mathematics for deployment in rural and outlying areas. Low salaries cannot be increased without an across-the-board rise in the civil service, which is not affordable. Field allowances are possible, sometimes in kind such as the provision of teacher quarters. However, the size of the allowances is not sufficient to attract the numbers and quality of teaching staff needed. The evaluation mission was told by the Sabaragamuwa Province Department of Education that field allowances are set centrally, so are out of their control.

30. An important feature to clients is the allowance of up to 25% of financing as advance disbursement, up to 20% for financing prior results, or a combination of the two not exceeding 30%. All RBL programs provide for this except Sri Lanka’s Education Sector Development Program. This RBL does not provide for advances, and this reportedly creates challenges for the government in meeting the cost of achieving DLIs before the ADB reimbursement takes place. On the other hand, Sri Lanka’s Skills Sector Enhancement Program provides for 20% of total financing to cover prior results to support government actions that are essential to initiate sector reform, such as (i) approval of the amendment to the Tertiary and Vocational Education Commission Act to strengthen the quality assurance system, (ii) signing of two
memoranda of understanding with private sector institutions to initiate private sector engagement in TVET provision, and (iii) approval of cadre positions for the Sector Development Division to strengthen sector coordination and management. The difference is likely because the Education Sector Development Program was the first RBL approved, and advance disbursement was omitted to facilitate rapid approval of the operation.

31. The fourth question is whether the proposed measures to strengthen the expenditure framework are appropriate to address risks and shortcomings. Again, in most cases the measures seem appropriate. Yet there were cases where concerns are raised. For example, in Nepal, risks are lack of a medium-term expenditure framework, weak links between policy and budget, delayed budget transfers to schools, and lower non-salary expenditure for schools than expected. Other risks not cited could include insufficient overall budget allocation (if costing is not correct) and inadequate salaries and benefits to fill key positions with qualified staff. Risk mitigation includes more robust medium-term expenditure frameworks, improved work plan, and allocation of district level resources using results based financing. These measures need to be carefully monitored as it is not clear they will work, particularly if it is hard to attract high quality key staff; costing uncertainty is there as well.

32. In the case of Supporting Kerala’s Additional Skill Acquisition in Post-Basic Education Program in India, the proposed handing over of O&M of community skills parks to a private sector management service provider is an innovative proposal. However, PPP agreements can be risky, particularly if government clients have no prior experience with them. Going forward, ADB technical assistance will be needed to provide experienced support to the client to ensure that this work is successful.

33. To summarize, expenditure frameworks are broadly clear and well costed, achievable, and likely to be sustained. They show value addition by ADB stemming from its previous experience in the sector, and the flexibility to incentivize priority results, while channeling funding where it is considered most needed and appropriate by governments. Some questions remain on funding of program costs after the completion of the RBL, particularly when the underlying government program continues for a long period after the RBL is completed. There are also examples of lack of clarity that could affect results, such in the Public–Private Partnerships Demonstration Program to Transform Delivery of Elderly Care Services in Yichang, Hubei in the PRC, where it isn’t clear whether the PPPs would be with a private or state-owned company.

Quality of Fiduciary Assessments.

34. This section addresses two main questions. First, were the fiduciary assessments of overall and program financial management, procurement, and fraud and corruption systems adequate to ensure that program funds will be used for intended purposes? Overall, fiduciary assessments give reasonable assurance of program systems that are functioning well, assuming mitigating measures are taken when there are problems. However, capacity development standards and staff incentives could be better defined, and most assessments of fraud and corruption prevention have moderate to serious shortcomings.

35. All RBL programs carry out separate assessments in financial management, procurement, and anticorruption, although most provide only the summary overall fiduciary assessment as a linked document to the report and recommendation of the President. There are references to PEFA assessments when these are available, including some at the provincial level. Nepal’s Supporting School Sector Development Program also drew on a public expenditure tracking study, support from the education management information system, social audits by parent teacher associations, which are mandatory for release of funds to community schools, and financial audits of schools.

36. In some cases, where there were shortcomings in mainstream systems, the implementing agency had already acted to address them before the RBL. For example, in the case of Pakistan’s Access to Clean
Energy Investment Program, Punjab has outsourced the implementation of the solar PV units. A private company, wholly owned by the Government of Punjab, Quaid-e-Azam Solar Power, has been appointed to take a lead role, with a project management unit dedicated to the solarization subcomponent. The Government’s Implementing Agency has also appointed a private firm from Germany, Lahmeyer, to help to review the bidding documents during the prequalification stage and the procurement of companies for the solar installation, and another firm, Engineering Consultancy Services Punjab, to help prepare the legal documents.

37. A common shortcoming across RBL operations is the assessment of fraud and corruption. Most assessments focus on laws, decrees, and regulations, rather than on actual practice. There are few references to publicly available information relevant to the functioning of program systems, for instance, Transparency International. Various information on this could be triangulated.\(^{18}\)

38. Armenia has joined the open government partnership and actions taken by Ministry of Education and Science include a complaint hot line, and a manual on education against corruption. However, there are also shortcomings. For example, officials and politicians and their relatives have control over private firms through hidden partnerships, leading to manipulation of procurement and the bidding system. Transparency International found nearly 60% of citizens surveyed think that political parties and parliament are corrupt or extremely corrupt.\(^{19}\)

39. A second question is: are the proposed measures to strengthen program fiduciary systems and governance adequate to address their risks and shortcomings? Measures are proposed in the three fiduciary areas. They may be included as conditions in the loan agreement, as DLIs, PAPs, and as risk mitigating measures. In the areas of financial management and procurement, the proposed measures are broadly reasonable. Since most of the RBL programs assessed have only been under implementation for a brief time, any assessment of the actual adequacy of proposed measures can only be preliminary.

40. IED’s survey of program team leaders found that almost 90% found RBL programs moderately to extremely useful in reducing transaction costs. However, ADB and other development partners have little evidence as to whether the intended benefits from the use of program systems—fewer delays in implementation, lower transactions costs, and improving ownership—is having any leverage effect on other government spending. These effects might only reveal themselves over a longer period, and could be analyzed through a series of public expenditure reviews in participating countries.

41. In the fraud and corruption area, in addition to measures specific to the area such as enhancing the complaints function, international experience shows that measures taken to strengthen financial management and procurement (e.g., transparency, complaint handling, use of standard bidding documents) will also help reduce fraud and corruption. However, because of weaknesses in the fraud and corruption analysis discussed above, it is difficult to assess the efficacy of proposed measures in the specific programs under focus.

42. Another shortcoming of many RBL programs is that the proposed capacity development measures are not fully described. In many cases, the only metric used is the provision of training in critical areas. There is considerable evidence that capacity development is more effective when there is rigorous follow-up to ensure the expected results of the training are forthcoming, such as certification achieved, successful performance on testing at completion, or follow up after a specified period to assess improvements in trainees’ job performance in areas related to the training.\(^{20}\) More explicit provision for such measures, including sustainability once the RBL is completed, would have strengthened the RBL programs.

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\(^{18}\) Transparency International often discusses corruption in public procurement in countries.


43. An additional shortcoming is that, while fiduciary measures that are part of DLIs are regularly monitored and reported on in supervision reports, there is somewhat less monitoring of other measures in the program action plan, although this situation is improving. IED's review of the initial and most recent supervision mission reports for Supporting Kerala’s Additional Skill Acquisition in Post-Basic Education Program and Supporting National Urban Health Mission, both in India, found no mention of progress on PAPs. Reports on the School Seismic Safety Improvement Program in Armenia mention some PAP issues, but don’t fully review progress. For Supporting School Sector Development Program in Nepal and Senior High School Support Program in the Philippines, there was no mention of PAPs in the initial report, but they are fully covered in the latest report. All fiduciary measures set out in RBL documents are assumed to be important for ensuring resources are used for the intended purposes, and should be subject to regular progress reports unless evidence is provided that the measures are no longer needed.

44. In the case of the Sustainable Transport Infrastructure Improvement Program in Solomon Islands, ADB and its cofinancing partner DFAT are both investing in extra supervision time to support the effective functioning of National Transport Fund systems. This includes the posting of an ADB infrastructure specialist in Honiara who had previously supported RBL programs in Sri Lanka, and DFAT’s requirement to issue no objection letters at different stages of the procurement process. The Ministry of Infrastructure Development told the evaluation mission that they didn’t support this process, since it reduced government ownership. On the other hand, DFAT explained to the evaluation mission that letters were produced in 1–2 days, and that MOFT disbursed National Transport Fund payments faster than other payments because of this extra scrutiny.

45. In the case of Sri Lanka’s Education Sector Development Program, an unusual issue arose in procurement. School buildings (two-story science laboratories and three-story technology faculty buildings) were procured using single source contracting drawing on firms registered with the Association of Sri Lankan Contractors, using a fixed price contract with a standard building design. This deviation from competitive bidding was approved by the Cabinet. ADB’s annual fiduciary review looked at a limited number of sample contracts, which include both single source and competitively sourced contracts, and found no clear evidence of large differences in contract price between them for the same design of building, and site visits found no difference in quality. Disbursement under DLI9 was held up to ascertain that less than 50% of audited contracts, including these sole source ones, had adverse findings. Based on this review, it was determined that Ministry of Education had met the 2015 requirement of the DLI that less than 50% of audited contracts had adverse findings, so ADB disbursed.

Summary of Findings and Recommendations

46. ODA is only a small part of total financing to developing countries. ADB and other development partners are moving towards new approaches, including pilot-testing, innovation, and learning to add greater value. One such approach is piloting the use of country fiduciary systems. Results-based lending uses program systems applying to specific programs, which may be higher quality than those for other programs. As a result, ADB hopes to gain in-depth knowledge on the program systems supporting a sector, while DMCs gain greater understanding about how to improve their own systems, and to get greater impact of their programs in the medium to long term, so that using program systems becomes the norm.

47. IED has assessed 12 RBL programs approved by the end of 2016 regarding the quality of expenditure frameworks and fiduciary assessments, and the appropriateness of the capacity development and other measures to strengthen systems and practices. RBL is a learning-by-doing approach shifting from direct project financing to supporting results. It seeks to improve the program systems for an entire DMC program, complementing other ADB instruments to scale up program systems, and deliver DMC priorities around results.
48. There are many assumptions embedded in the RBL analytical framework. First, it is assumed that working with program systems will help strengthen them; there is ample evidence that this can be the case. Second, it is assumed that the costs of achieving the intended results can be and are being accurately estimated up front.

49. Third, it is assumed that it is possible to carry out a fiduciary assessment, and come to a clearly formulated, reliable conclusion. In cases where fiduciary weaknesses are apparent, it is also assumed that capacity development and risk mitigation actions can be identified and that they will be successful. A further challenge underlying the assumption behind system strengthening is the distinction between strengthening formal and functional aspects. The evaluation has looked carefully at the measures proposed to ensure a good balance of formal and functional. If measures are only formal, there could be good laws and regulations in place that aren’t implemented as intended, so they would not lead to an adequate fiduciary environment. Care must be taken also to ensure that more challenging functional measures are also adopted successfully.

50. Bringing this analytical framework first to bear on the quality of expenditure frameworks, there was overall an adequate definition of the RBL’s program’s expenditure framework, including the scope and boundary vis-a-vis the broader government program. Questions can arise when the expenditure framework covers a long-time period, creating challenges for costing and estimating funds availability. In one case, there was a question as to whether a PPP partner was private or state-owned, with implications for financial sustainability and efficiency.

51. Most RBL programs also clearly articulated ADB's value added. In some cases, ADB had previous experience in the sector, providing help in costing, and in managing fiduciary risk. In another case, the RBL program allowed ADB to disburse based on achievements in improving transport infrastructure maintenance, while the government could use the funds for eligible investment expenses under the program, in compliance with its debt management strategy which does not permit the use of debt for recurrent costs. Value addition is also evident in the shift from grants based on unit costs to performance- and needs-based grants, as happened in Nepal’s Supporting School Sector Development Program, and in the willingness to try new approaches as in Sri Lanka’s Skills Sector Enhancement Program, which piloted performance-based contracting of private training providers to deliver training and job-placement services.

52. In most cases, the RBL financing plans seemed to be sustainable, and the measures proposed to mitigate risks seem appropriate. However, some risks seem to have been systematically underestimated, such as recruiting highly qualified (and hence much in demand) financial management and procurement staff and retaining them in key positions, particularly outside major urban centers.

53. Moving on to the fiduciary assessments, in general they give reasonable assurance of program systems that function well, assuming that mitigating measures are taken when there are problems. In some cases, where there were shortcomings in mainstream systems, the implementing agency had already acted to address them before the RBL. A common shortcoming was in the assessment of fraud and corruption. Most assessments focus on laws, decrees, and regulations, rather than on actual practice. There has been little or no reference to publicly available information on fraud and corruption.

54. Mitigating measures are proposed in the three fiduciary areas analyzed in the assessments. They may be included as conditions in the loan agreement, as DLIs, PAPs, and as risk mitigating measures. In the areas of financial management and procurement, the proposed measures are broadly reasonable. Since most of the RBL programs assessed have only been implemented for a brief time, any assessment of the actual adequacy of proposed measures can only be preliminary.

55. A concern for many RBL programs is that the proposed capacity development measures are not fully described. In many cases, the only metric used is provision of training in critical areas. There are few
details provided on the expected results of the training, such as certification achieved, successful performance on testing at completion, or follow up after a specified period to assess improvements in trainees’ job performance in areas related to the training. Another concern is that there seems to be no provision in RBL programs to monitor whether the use of program systems reduces delays in project implementation, reduces transactions costs, improves ownership, or has a leverage effect on other government spending. This is surprising, since the rationale for adopting RBL programs is that these benefits would result.

56. An additional concern is that, while fiduciary measures that are part of DLIs are regularly monitored and reported on in supervision reports, there is less evidence of monitoring of other measures in the PAP. All fiduciary measures set out in RBL documents are assumed to be important for ensuring resources are used for the intended purposes, and should be subject to regular progress reports unless evidence is provided that the measures are no longer needed.

57. A final observation is that staff are instructed to use their own judgement in estimating the overall risk rating for a proposed RBL. The overall risk rating is based on the team’s judgement of risk under six categories: results, expenditure and financing, fiduciary, safeguards, operating environment, and other. The overall rating is not meant to be an average of all the ratings, but rather based on the team’s judgement in light of the program outcome to be achieved. Thus, there can be cases where the overall risk rating may be less than the rating for fiduciary risk. This is the case with Uzbekistan Rural Housing, an RBL program approved in 2017 and thus not one of the 12 being evaluated here. In that case, the fiduciary risks are assumed to be high, particularly in the area of procurement, while the overall risk rating is substantial, which is the same as that of eight of the 12 RBL programs approved to the end of 2016. While ADB’s prior experience with the implementing agency gives some assurance that proposed fiduciary risk mitigating measures will be successfully carried out, the team needs to exercise caution that progress in risk mitigation is carefully monitored during supervision missions.

58. Four conclusions and suggestions arise from this analysis:

59. First, a key assumption of the RBL modality is that working with program systems will help to strengthen them. RBL is a form of performance or program-based budgeting, where allocations are explicitly linked to outputs and outcomes delivered. There is ample evidence that such reforms haven't worked in fragile contexts on a broad scale; the question is whether they can work in the more limited setting of an RBL program. In the RBL programs reviewed, the evaluation found early evidence that some RBL program systems have been strengthened based on progress in relevant DLIs and PAP actions in supervision reports. It would be instructive to gather evidence more systematically to assess this, possibly through repeat PEFA assessments to see if the strengthened RBL program systems can be scaled up later beyond the program boundaries.

60. Second, there is a need for a comparison between using program systems for a sector program (i.e., program systems) and the traditional approach of parallel fiduciary controls managed by development partners. It would be very useful to undertake a comparison of both types of project administration in the same sector and country to assess their relative benefits, inefficiencies, and fiduciary risk. One could also add hybrid models to the mix, such as the Solomon Islands case, where a development partner is carrying out prior review of country procurement processes and decisions. Other development partners have experimented with hybrid approaches adopting DLIs within investment projects in order to help DMC clients gain experience and comfort with use of DLIs and results-based approaches within investment projects before adopting the new modality. Knowing both the costs and the benefits of using program systems can help ADB better decide how and when to phase in the new modality in different country and sector settings.

21 Schiavo Campo and Tommassi, footnote 13, p. 12.
61. Third, capacity development support is essential in many country settings to achieve minimum standards of fiduciary control but such support is not always designed carefully nor adequately resourced. RBL programs should ensure this support is effective and efficient and relevant by drawing on the diagnosis and capacity assessments of recipient organizations. The assessments should identify specific and measurable capacity-building objectives and spell out the support needed to achieve the objectives, including budgets needed, participant selection criteria, expected standards of learning accomplishment (e.g., testing and certification), follow up support to assess ability of trained staff to use newly acquired skills to carry out essential tasks, and measurable indicators of success.

62. Fourth, measures to address fiduciary weaknesses set out in loan agreements, DLIs, PAPs, and risk assessments should be systematically monitored during supervision. The evaluation found that while measures that are part of DLIs are regularly monitored, there is less monitoring of other measures. Since all measures were deemed important as part of fiduciary assessments, they should all be regularly reported on in supervision reports, or evidence provided that specific measures are no longer required.