State Building in Conflict Affected and Fragile States: A Comparative Study

Timor-Leste and Afghanistan

Public Finance and National Accountability

Technical Working Paper:

Trend Analysis of Fiscal Performance Improvement and Cost-Effectiveness

ISE Institute for State Effectiveness

Acronyms

ACER	Average Cost-Effectiveness Ratio
CBA	Cost-Benefit Analysis
CEA	Cost-Effectiveness Analysis
CER	Cost-Effectiveness Ratio
DFID	Department for International Development
FRI	Fiduciary Risk Index
GDP	Gross Domestic Product
ICER	Incremental Cost-Effectiveness Ratio
IDA	International Development Association
IMF	International Monetary Fund
ODA	Official Development Assistance
ODI	Overseas Development Institute
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PI	Performance Indicator
QALY	Quality Adjusted Life Year
Rev	Revised
Ri	Risk Index
SIGAR	Special Inspector General for Afghanistan Reconstruction
TCER	Timewise Cost-Effectiveness Ratio
UK	United Kingdom
UNRWA	United Nations Relief and Works Agency
WDI	World Development Indicators

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EXECUTIVE SUMMARY

Introduction

This analysis provides a comparison of fiscal performance improvements over time for Afghanistan and Timor-Leste. It reviews changes in the quality of public financial management systems as revealed by Public Expenditure and Financial Accountability (PEFA) assessments, development and fiduciary risk analysis and other indicators, including by looking at the cost effectiveness of aid interventions in both countries. ***It also compares systemic fiscal performance with other g7+ countries.***[1]

The purpose of this paper is to assess the quality of public finance reforms and the value for money achieved via aid. In particular, the purpose is to assess:

i. **Where Timor-Leste and Afghanistan sit in terms of the quality** of their public financial management systems;
ii. **How far these countries have come over time** in terms of system quality; and
iii. **How much it has cost donors to help these countries improve**.

The analysis was structured around three periods, an early period from around 2002 to 2006, a middle period from 2006 to 2010 and a later period from 2010 to 2015.[2]

Underpinning the analysis is a hypothesis that investing aid money in public finance systems should lead to stronger public finance systems, as measured by whatever standard of quality and strength available. There are many ways to measure quality and strength in public finance systems. One of the generally accepted ways is through PEFA and its proposition that strong public expenditure and financial accountability systems deliver better outcomes and value for money. This paper accepts that proposition and then tests how well aid has been used in the public finance sector to achieve that desire result of stronger and more robust public finance systems.

Whether aid is actually used to improve public finance systems is a different question. There is a case that can be made that aid to finance ministries might be more about keeping a country afloat, rather than building better institutions and systems. We would argue that if aid is not being used strategically to help deliver successful reform, the very fundamentals that are driving a crisis will not be properly addressed: ***The way out of a crisis is to reform not to keep investing in the status quo.***

Results

The analysis reveals that Timor-Leste and Afghanistan are doing relatively well in developing their public finance and national accountability systems. Both countries are at about the same standard. PEFA trend analysis reveals that they both started at about the same standard at the beginning of the century (around a simple PEFA average of "D"). Timor-Leste's improvement, however, has been steady, while Afghanistan's was rapid at first but has then plateaued in recent times. Both Timor-Leste and Afghanistan have leading systems compared to other g7+ countries, and rate well in certain areas (at around a "C").

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[1] This paper should be read in conjunction with the paper *State Building in Conflict Affected and Fragile States: A Comparative Study Timor-Leste and Afghanistan - Public Finance and National Accountability (2016)*.

[2] This paper is aimed at policy makers and development practitioners and is quite technical in its approach. A working knowledge by the reader of the PEFA framework and concepts like fiduciary and development risk are assumed.

Development and Fiduciary Risk Analysis reveals Timor-Leste and Afghanistan's relatively high standard compared to other g7+ countries. The analysis highlights that development risks - where we mean the risk of not achieving development goals - is much higher than fiduciary risks - where we mean the risk the money is wasted, stolen or misused. Development risks are shown to be substantial to high, while fiduciary risks are moderate to substantial (under a four-tier rating scale of low, moderate, substantial and high). On a positive note, both are falling over time, but the analysis shows that "how" reforms are structured and sequenced and the level of ownership by the Government appears to be a key determinant of how effective reforms to national systems are in achieving or contributing to development outcomes. In countries that are highly aid dependent the way development assistance is provided also has an impact on development outcomes, with analysis showing that prime facie there is a case that more use of national systems reduces both development and fiduciary risk.

The analysis also shows that Timor-Leste is more cost-effective in reducing fiduciary and development risks in most cases. Due to the large population differences, Afghanistan is more cost effective during some periods when results are presented in per capita terms. However, in the most recent period, Timor-Leste is more cost-effective on achieving reform gains even on a per capita basis. This corresponds to a period where Timor-Leste has become relatively independent of donors while Afghanistan remains heavily aid dependent.

Results also indicate that difficult reforms appear to take longer and are generally more expensive. In the very early years between 2002 and 2005 Timor-Leste was around three times more cost effective. Under a wide scope scenario – meaning aid funding purpose included aid for public finance management, decentralization and public administration sectors (narrow scenario is in brackets – meaning just public finance management) - and constant[3] cost it costs donors to Timor-Leste $153.8m ($18m) to secure an average half grade improvement in the simple average PEFA score, compared to Afghanistan, which costs $496m ($50m). For the later period, Timor-Leste was almost fifty (50) times more cost-effective than Afghanistan under wide cost terms and twenty-three (23) times under narrow cost terms. Timor's Timewise Cost Effectiveness Ratio (TCER)[4] was $214m ($42m), compared to Afghanistan's $10.5 billion ($1 billion) under wide cost (narrow cost) terms. The analysis shows that when conditions are right it takes around 3 to 5 years to improve PEFA scores by half a grade. This was the case for the majority of g7+ countries during most periods, including Afghanistan and Timor-Leste, save the later period between 2008-213 for Afghanistan, where results indicate that it would take over 13 years to achieve a half grade improvement.

In terms of per-capita[5] costs, Afghanistan becomes much more cost-effective compared to Timor-Leste in the early to middle periods. In the early years it cost Afghanistan's development partners $2 per person to help raise PEFA by half a grade, in Timor-Leste it cost development partners $17 per person. For the middle period it was $5 compared to $45, and for the late period, Timor-Leste became more cost-effective in per capita terms at $35 compared to Afghanistan's $38.

[3] Which means – costs adjusted for inflation.

[4] A Timewise-Cost-Effectiveness Ratio (TCER), developed for this analysis, is the sum of the annual current costs adjusted for inflation over the change in effect. The cost calculation, is equivalent to the sum of the constant costs – or constant aid disbursements. Incremental costs are those additional resources provided through aid – on top of non-aid or government own-source financed reform, which includes activities funded by budget support.

[5] Per capita in terms of country population.

Discussion

Working in conflict and fragile states is difficult for everyone: government officials, elected representatives, donors and contractors. This study reaffirms this view. There are various implications from this assessment, and there are methodological issues and limitations to the approach used here in understanding progress, performance and value for aid money.

On the question of the resilience of public finance systems - it appears to work in two ways. It can mean resistance to change for the better or worse. In other words, while it may be difficult to build better systems, it may also be difficult to change them. People have a tendency to resist change, and routine processes are routine for a reason. This study reveals that when the conditions are right progress on reform and positive change can happen relatively quickly over a few years. Examples are Timor-Leste, once aid-dependency was reduced, and Afghanistan in the early years, when there was essentially an open canvas and plenty of resources. At the same time, however, we see that when the conditions are not right, progress is slow and uneven. Such as in Afghanistan during the last 5 years when the number of development projects increased and political will for reform was arguably lower. Moreover, we also see that in highly difficult environments where conflict is pervasive and political settlements are tenuous, public finance system resilience can break down.

The wider analysis of g7+ countries reveals that reform efforts are volatile. Success over a number of years does not mean success in subsequent years. Of course this raises issues of the importance of leadership and other factors such as the drivers of institutional culture. Further research is warranted to see if volatility in reform progress is higher in fragile and conflict affected countries, compared to other groupings of countries. [6]

The issue of value for money from aid investments is an important one to explore further. On the face of it, this analysis shows some negative cost-effectiveness ratios that indicate that the common alternative course of action – "to do nothing" – may be better than intervening at all. Spending tax payers' money to go nowhere or even to go backwards does not appear to be good fiscal, aid or foreign policy. However, there are important considerations. The lack of counterfactuals is a key limitation. The alternative approach has not been modelled here, and nor has the consequences of no intervention. For example, financial assistance could have prevented catastrophic collapses of public finance systems that keep governments working, cities running and communities functioning. Here, we see that the limitations of the data. We don't know what the money is actually being spent on – e.g. funds may not be targeted at PFM, but on political settlements.

In a way, some of the results revealed in this paper indicate that the international community may well be paying to avoid adverse effects of worse outcomes that could occur in the absence of assistance. There might well be the view that the investment is to just keep "heads above water". In other words the cost is written off as the sunk cost to keep things from falling apart or in other words, the cost of fragility. The reality is more likely to be that we're not doing enough to focus efforts on the right reforms and in the right way. Nor are we focusing enough on the foundations that help institutions create cultures of high performance, and help public services and public servants be self-reliant and accountable for successes and failures. In other words it is not "what" is being done, it is "how" we're doing it.

[6] There could well be data quality issues compromising results. PEFA is notoriously subjective, especially in the early years of its implementation. There were often debates in PEFA discussions on whether performance scores were a D or an A, let alone debates on half, grade differences.

We still have many unanswered questions. Does using country systems to improve them in the right way deliver better results at less cost – is sector budget support better than projectized aid delivery? Does project-based aid actually reduce exposure to fiduciary risks or even reputation risks? Could the use of different methods of aid delivery and donor-recipient accountability frameworks have led to better outcomes – is performance based aid better than traditional in-kind Technical Assistance projects? Could better accountability and risk sharing between donors and recipients set better conditions for success – should a mix of fixed and variable performance payments be prioritized over traditional aid delivery systems? More research is warranted, though intuitively these questions appear to be the right ones to be asking.

Importantly this analysis stresses that development risk should be much more of a concern for donors than it currently is, especially when compared to demonstrable concerns over exposure to fiduciary and reputation risks. This is not just in terms of probability, but also in terms of value for money. Not getting good development outcomes from billions in aid investments is a bigger issue than avoiding adverse domestic consequences of corruption. No donor, however, has been able to win that argument at home. A solid program of analysis of cost-effectiveness of aid interventions and development risk assessments would, however, help the case and build the evidence base.

By focusing more on development risk, aid must be flexible and modalities need to shift from project based aid, to flexible performance orientated aid. Similarly, a focus on self-reliance and taking on the roadblocks and bottlenecks to reform, reinforces the idea that efforts at using country systems - budgets, accounts and audits - must be ramped up. We are still a long way from aid dependent countries having budgets that are an instrument of government policy, rather than a type of political settlement tool, auction-based, or just an aggregation of ambit claims, while donors manage resource allocation and are responsible for reporting on performance.

INTRODUCTION

This paper provides a comparison of fiscal performance improvements over time for Afghanistan and Timor-Leste. It provides the results of a comparative cost-effectiveness analysis of aid interventions. It also reviews changes in the quality of public financial management systems as revealed by Public Expenditure and Financial Accountability (PEFA) assessments, development and fiduciary risk analysis and other indicators. It also compares systemic fiscal performance with other g7+ countries.

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1. **Where Timor-Leste and Afghanistan sit in terms of the quality** of their public financial management systems;
2. **How far these countries have come** over time in terms of system quality; and
3. **How much it has cost donors** to help these countries improve.

Underpinning the analysis is a hypothesis that investing aid money in public finance systems should lead to stronger public finance systems, as measured by whatever standard of quality and strength available. There are many ways to measure quality and strength in public finance systems. One of the generally accepted ways is through PEFA and its proposition that strong public expenditure and financial accountability systems deliver better outcomes from public spending and better value for money. This paper accepts that proposition and then tests how well aid has been used in the public finance sector to achieve stronger and more robust public finance systems.

Whether aid is actually used to improve public finance systems is a different question. There is a case that can be made that aid to finance ministries might be more about keeping a country afloat, rather than building better institutions and systems. We would argue that if aid is not being used strategically to help deliver successful reform, the very fundamentals that are driving a crisis will not be properly addressed: ***The way out of a crisis is to reform not to keep investing in the status quo.***

Another hypothesis that underpins this work is the belief that development risk – by which we mean the risk of not achieving development goals, should be a much greater concern to donors, than efforts to reduce exposures to reputation and fiduciary risks. **(**See Box 1 below on page 9 for expanded definitions including for other risks). By focusing on both development and fiduciary risk, we aim to increase attention on building systems and institutions that deliver self-reliance, pathways out of aid dependency, and getting public finance systems to work well for governments and citizens. Moreover, we believe that there has been too much attention on fiduciary risks, which biases aid delivery towards ways that bypasses country systems and institutions, which in our opinion should be primary targets for any donor interested in delivering cost-effective aid.

Box 1. Defining Key Risks

Fiduciary risk is the risk that aid or government funds: i) are used for unauthorized purposes; ii) do not achieve value for money; or ii) are not properly accounted for. The realisation of fiduciary risk can be due to a variety of factors, including: lack of capacity; inappropriate procedures and systems; weak competencies or knowledge; bureaucratic inefficiency; active corruption; and or weak or absent laws and enforcement. Perceptions of fiduciary risk can be influenced by expert opinion or an evidence based quantification of fiduciary risk.

Development risk is the risk that development assistance or government/agency resources will not achieve results – particularly development objectives and long term goals including economic growth and poverty reduction - and enabling objectives such as reform and capacity development. Development risk is influenced by the level of administrative burden placed on governments /agencies by donors as well as compliance costs associated with complex donor procedures that do not match technical capacities of individuals and institutions. There is a position that capacity development and reform can be better supported by appropriate use of various country system components. The idea is centred on the principle that "to improve a system you should use the system". Perceptions of development risk can be influenced by expert opinion or an evidence based quantification of development risk.

Sovereign financial risk is the risk that a loan will not be repaid in full or on time. It is a lending risk and is assessed differently through fiscal and debt sustainability analysis and other tools. Credit rating agencies constantly form and modify opinions on a Government's credit worthiness based on evidence (e.g. Article IV consultation reports, World Bank reviews and publications and Government economic and fiscal reports), media reports, and information gained through their network of sources and their own analysis. Higher assessed risks by these agencies may result in an increase to the cost of borrowing for the country, the extent to which is subject to other factors, including market reactions, though it is more likely if loans are directly linked to credit rating. Management of sovereign risk is handled differently to fiduciary risk management, though good management of both risks mitigate both.

Reputation risk is the risk that perceptions of poor management of funds or poor levels of development effectiveness (whether real or otherwise) will have adverse consequences. Reputation risk applies to donors, governments and agencies. In terms of donors, adverse consequences include: i) deterioration in the level of support for foreign aid by tax payers, central agencies, members of parliament, development ministers and cabinet; ii) criticism of aid management; and iii) deterioration in diplomatic relations with a partner country and international finance institutions. In terms of country governments, reputation risk is relevant as they are ultimately accountable to their citizens for the efficient and effective use of all national resources. Reputation risk can influence sovereign risk and perceptions of fiduciary and development risk. For agencies, adverse consequences include loss of management control and additional administrative burdens arising from heightened external scrutiny and criticisms at multiple levels.

Political Risk (or geopolitical risk) generally refers to difficulties agencies, firms and/or governments may face as a result of political decisions or "any political change that alters the expected outcome and value of a given economic action by changing the probability of achieving business objectives." Political risks are hard to quantify due limited sample sizes or case studies when discussing an individual nation, though certain risk rating agencies attempt this.

Drawn from Shand, 2005[7] and for political risk: DiPiazza and Bremmer, 2006[8]

The paper is structured around four sections. Section A provides the methodology and results of the country comparisons of PEFA results over time for Afghanistan and Timor-Leste, and compares them to other g7+ countries. Section B goes further by analysing the trends in quantified development and fiduciary risks. Section C, provides the results of a trend and cross-country study looking at the cost-effectiveness of aid interventions to improve PEFA scores and reduce risks. The paper ends with a discussion on the implications for development policy in

[7] Shand, (2005), "Managing Fiduciary Issues in Budget Support Operations" In Koeberle, Stavreski, and Walliser (ed), 2005, "*Budget Support as More Effective Aid*?" World Bank, Washington DC

[8] DiPiazza and Bremmer, 2006, "*Integrating Political Risk Into Enterprise Risk Management*", PricewaterhouseCoopers and Eurasia Group, New York, USA

terms of: i) pursuing implementation methods that deliver value for money; ii) recognizing progress is context specific and can be slow, expensive and uneven; and iii) self-reliance, sustainability and value for money can be complimentary. A discussion on the limitations of the assessment and future areas for research is also provided.

A. Country Comparisons: PEFA

This Section reviews the trends in PEFA scores for Timor-Leste and Afghanistan, and compares them to other g7+ countries. The assessment provides an insight in to the relative effectiveness of aid interventions that are aimed at helping governments build stronger public finance and national accountability systems.

Methodology

In order to facilitate comparative analysis, g7+ country PEFA scores were converted to numerical values in line with common approaches, such as in Fiduciary Risk Assessments and PFM system analysis undertaken by DFID, other comparison reports by the World Bank, the IMF and others (see PEFA index[9] and Delorenzo[10]). Numerical conversions are as follows: A=4, B=3, C=2 and D=1, with + scores given an additional 0.5. These are summarized in Table 1 below along with the two different approaches to categorizing risk under a four tier method. Zero-to-one (0-1) scale equivalents are also provided.

Table 1: Numerical Conversion of PEFA Scores and Risk Categories

PEFA Score	**A**	**B+**	**B**	**C+**	**C**	**D+**	**D**
Numerical Value# (Avg. Equivalent)*	4 4-3.75	3.5 3.7499-3.25	3 3.2499-2.75	2.5 2.7499-2.25	2 2.2499-1.750	1.5 1.75-1.250	1 1.25-1
0-1 Equivalent (Range Equivalent)	0 0-0.83	0.167 0.830-0.25	0.333 0.250-0.417	0.500 0.4170-0.583	0.667 0.5830-0.750	0.833 0.75-0.9170	1.000 0.917-1

Risk Category 4 Tier Range DFID~	**Low** 4-3.25	**Moderate** 3.2499-2.5	**Substantial** 2.499-1.75	**High** 1.749-1
0-1 Equivalent	0-0.25	0.250-0.5	0.500-.75	0.750-1

 # Commonly used scale including IMF PEFA Index[9] *and De Lorenzo (2009)* [22] [11].
** Transition points determined by possible PEFA scores as equal spacing not possible under PEFA alpha + scoring methodology.*
~ Equal spacing (determined by four equal parts of 3 integers =0.75) with transition points determined by exact/unrounded score to achieve lower risk level.
^ Equal spacing (determined by five equal parts of 3 integers =0.6) with transition points determined by exact/unrounded score to achieve lower risk level.

There are recognized problems with averaging PEFA scores. De Lorenzo (2009)[22] pointed out that "the PEFA methodology actually measures very different things" and that the "use of averages is based on the assumption that all indicators are equally important". He went on to explain that "this might be problematic for a number of reasons. For some parts of the framework, for example, some indicators may actually be 'more important' than others". This is particularly relevant for fiduciary risk analysis. Simple averaging of numerical PEFA scores does not take into account indicators or dimensions that are more important to fiduciary risk than others. An effort to address this problem, means exploring results in different dimensions, such

[9] The IMF PEFA index uses PEFA ratings for the main 28 components and is based on an ordinal scale (A to D) which is converted into numerical values and then aggregated using equal weights. Therefore, PEFA scores (A,B,C,D) are converted into the four ordinal to numerical scores (4,3,2,1) – to assist with graphing results - , with "+" score given a ½ point. Equal weights are assigned to each of the 28 government PFM indicators. Non Rated (NR) and/or Non Used indicators are not used in the calculation. [19]

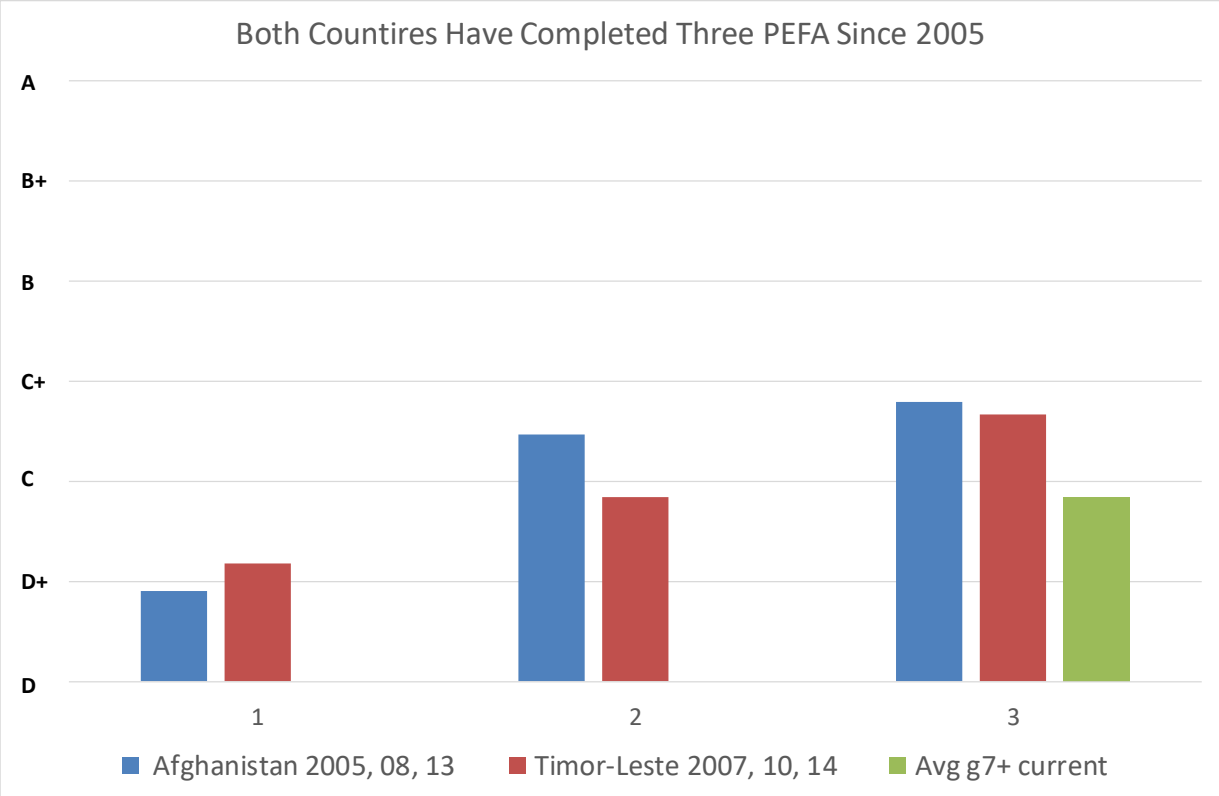
[10] De le Renzo, 2009, "Taking Stock: What do PEFA Assessments tell us about PFM systems across countries?", Working Paper 302, ODI, London, UK. (Accessed 23 November 2009)

[11] If applying standard risk quantification methodology of performance score (PI) x risk factor (importance of PI to fiduciary risk) then numerical progression should be reversed with A=1 and D= 4 if risk factors for example are: Low risk factor=1, moderate risk factor=2 and high risk= 3. This is so that intuitively higher numbers (and higher multiplied numbers) relate to higher risk.

as drilling down on components and different groups of performance indicators. This problem is also addressed in Section B, where Fiduciary and Development Risks are quantified, by essentially weighting some PEFA scores differently according to contribution to risk level and risk type.

Results

Figure 1. Three PEFAs Each



Timor-Leste and Afghanistan have both under taken three PEFA assessments (see Figure 1 above). Afghanistan completed them in 2005, 2008 and 2013, while Timor-Leste completed them in 2007, 2010 and 2014. Both countries started about the same level of around a "D+" simple average, and have progressed at around the same rate to around a "C+" average. Afghanistan made faster progress in early years then slowed down, while Timor-Lest has made steady progress since 2007. Performance of the two countries is well above the average for all g7+ countries latest PEFA assessments, which is around a "C".

Performance is different at the PEFA thematic level. Afghanistan is doing better on predictability and controls, credibility of the budget, while Timor-Leste is doing better at policy based budgeting and accounting. Donor practices significantly improved for both going from "D" to "C" over the period (see Figure 2 and Figure 3).

Figure 2. Afghanistan and Timor-Leste PEFA Improvements – in PEFA Space

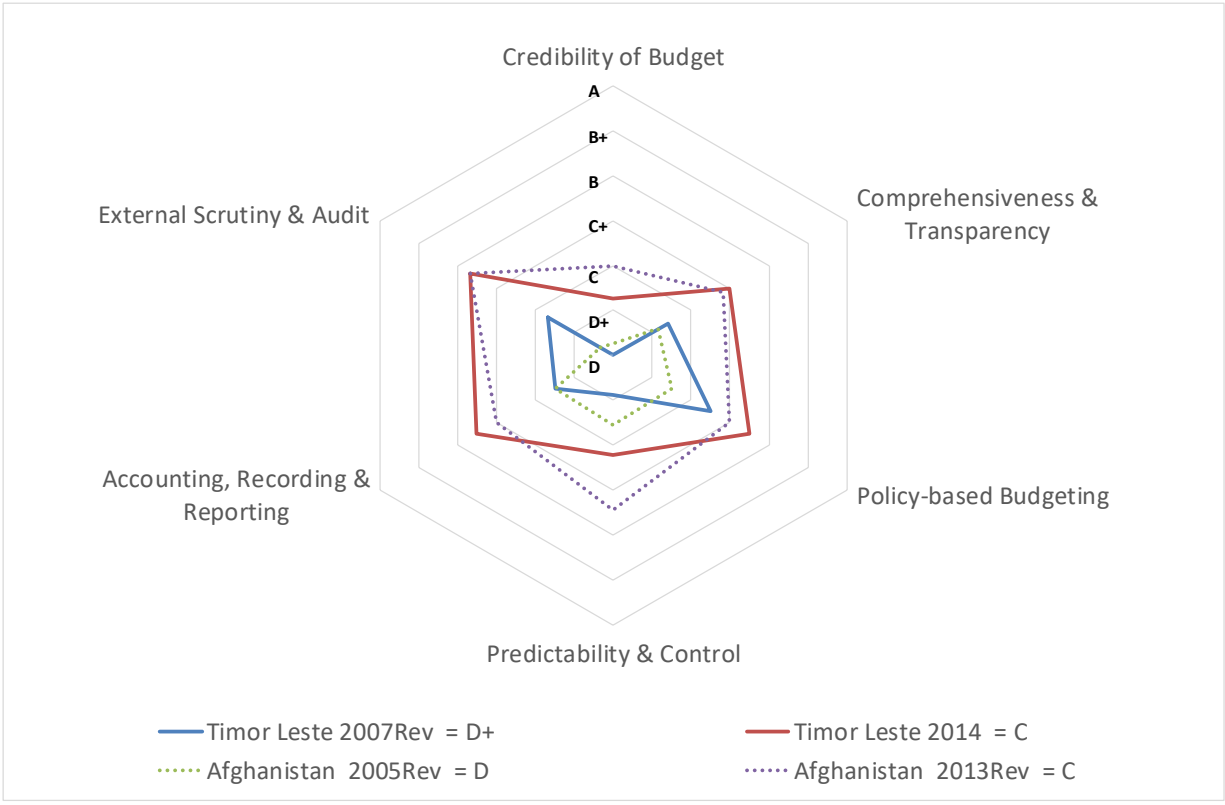


Figure 3. PEFA Improvements – by PEFA Theme: Early & Late Years

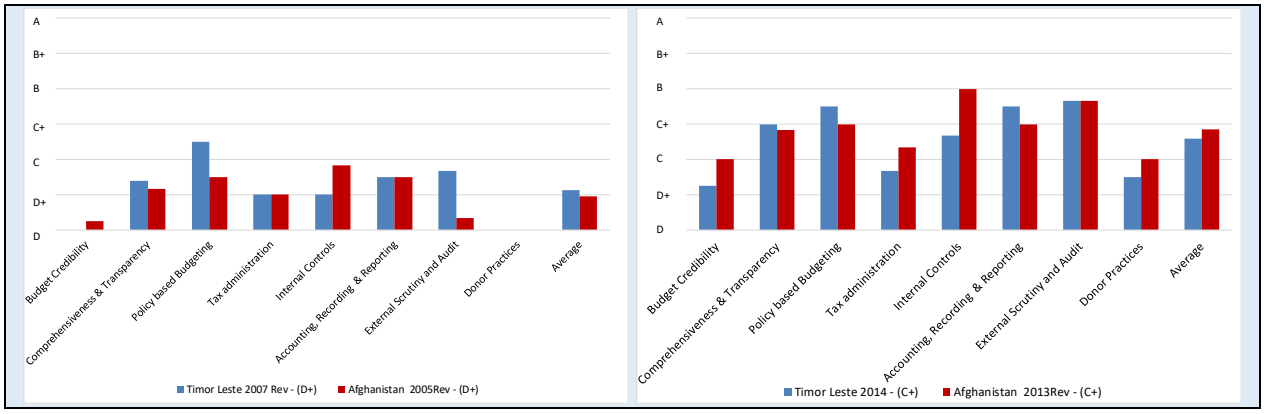
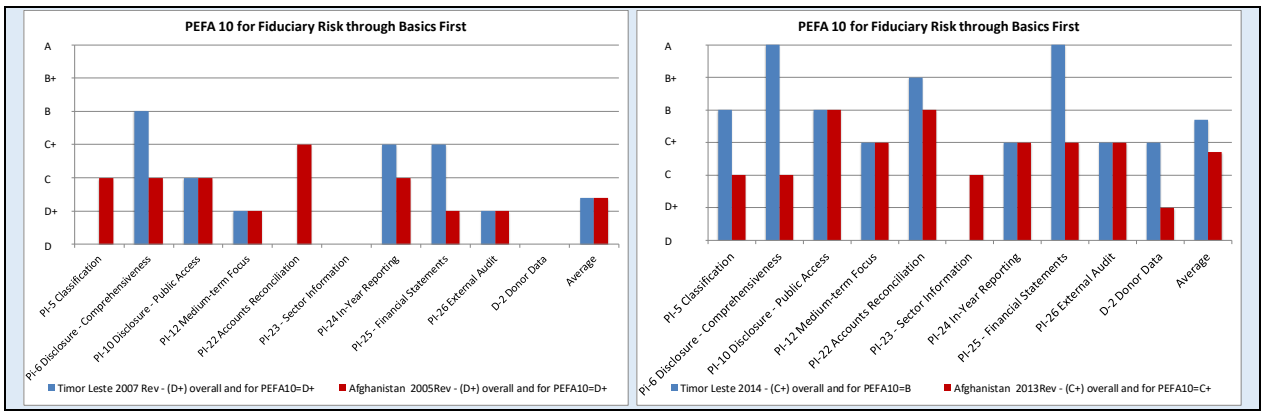


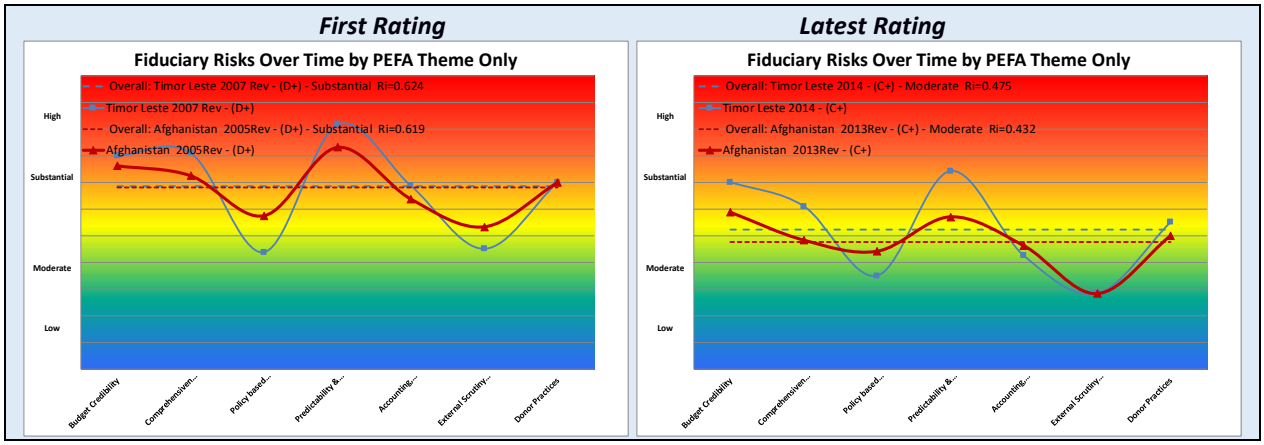
Figure 4. Afghanistan and Timor-Leste PEFA-10 Improvements



In terms of performance against the PEFA-10 subset, Afghanistan and Timor started at the same level, but Timor-Leste improved more over the period (see Figure 4). PEFA-10 is an approach that measures systemic fiduciary risk. It takes a subset of PEFA indicators as a proxy for fiduciary risks[12] based on the idea of "basics first" in accounting control. Major areas of difference are in Timor-Leste's progress on: i) classification systems; ii) budget paper disclosures; iii) accounts reconciliation; and iii) financial statements.

In terms of fiduciary risk reduction[13], both countries fell from overall substantial fiduciary risks to a moderate fiduciary risks based on assessed strength of fiscal management systems. Both countries have similar fiduciary risk profiles, with highest risk peaks associated with predictability and control, though this was an area where Afghanistan was still able to secure significant fiduciary risk reductions (see Figure 5).

Figure 5. Afghanistan and Timor-Leste Fiduciary Risk Comparisons



Development risks for both Timor-Leste and Afghanistan, are significantly higher than fiduciary risks, falling from high to substantial over the same period (see Figure 6). The major drivers of high development risk – by which we mean the risk of not achieving development objectives - for both countries are associated with various constraints to development. Some of the key reform objectives that would reduce development risk include:

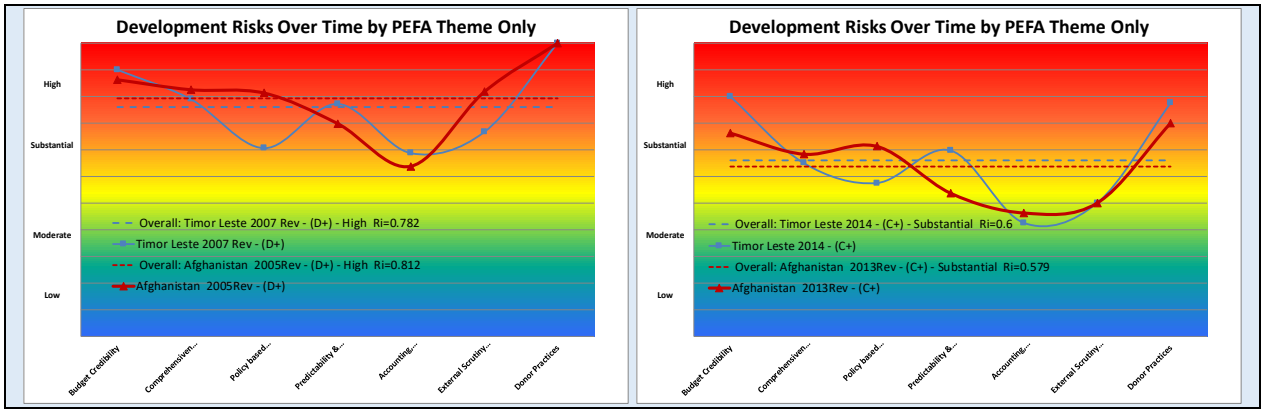
i. **Delivering an increasingly accurate and believable budget** – reducing the risk that medium term development goals will not be achieved and budgets are not auctioned off to the highest bidders;
ii. **Managing exposure to risks posed by public enterprises and reducing incidence of unreported expenditures** – reducing the risk of misallocation of funds from development to bail out or finance inefficient market operations;
iii. **Running effective policy-based budget process that uses forward year estimates of the costs of existing policies** and robust systems for costing and consolidating new policy proposals – reducing the risk that medium term development goals will not be achieved and budgets are not auctioned off to vested interests;
iv. **Targeting very weak tax collection systems** – particularly in tax arrears and reconciliation management – reducing risk of misallocation of funds for development due to less revenue raising and more leakage; and

[12] Hashim, 2015, "Presentation: A Practitioner's Guide for Setting Reform Priorities, Systems Design and Implementation", Phnom Penh, Cambodia.
[13] The fiduciary risk quantification method used is the same one used in the Development and Fiduciary Risk Assessments undertaken for Timor-Leste in 2012 and Afghanistan in 2015.

v. **Taking on the intractable problem of aid-induced fragmentation of fiscal management systems** – compromising the ability of a fiscal management system to work as intended: to be the continuous improvement cycle for government.

Comparability of budgets and accounts (or promises with results) and annual reporting of fiscal and non-financial performance remain a challenge in both countries, compromising the ability of the accountability system to deliver continuous improvement in fiscal and institutional performance – significantly increasing development risks. For development risks to be reduced, a government needs a budget cycle that delivers continuous improvement based around clearly specifying promises – what will be produced each year with a given level of government resources, with what actually happened. For the system to work, it should be easy for a lay person to pick up a budget paper and pick up an annual report and compare promises with results. If it is too difficult, then a continuous improvement system – a budget system - cannot operate well.

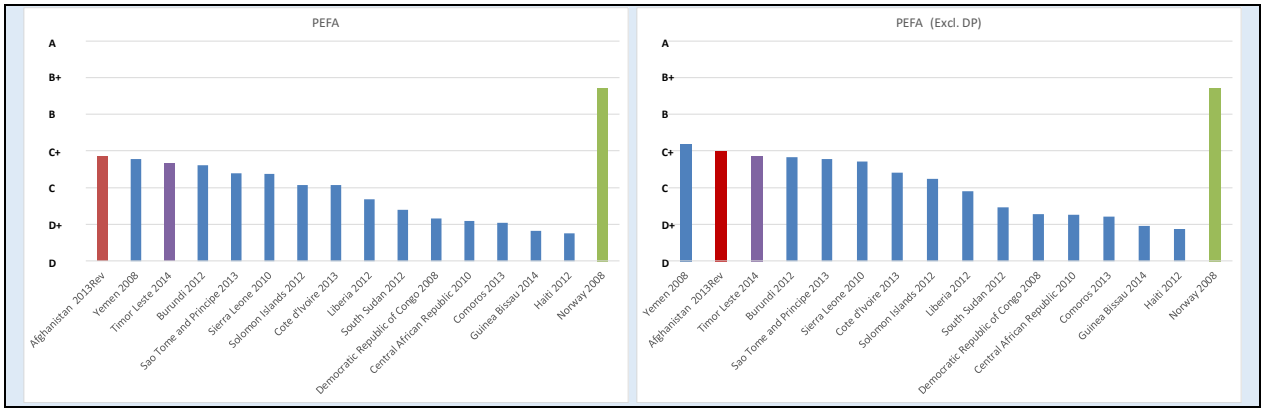
Figure 6. Afghanistan and Timor-Leste Development Risk Comparisons



g7+ Country Comparisons

Afghanistan and Timor-Leste are leading g7+ countries in terms of performance against PEFA. They both rate relatively highly on the g7+ league table of PEFA performance at a simple average of "C+", but are still some way off the best published result of Norway of "B+". Afghanistan is the top country in terms of simple average of all PEFA indicators including Donor Practices. Timor-Leste is third in this category Taking Donor Practices out of the average score, brings Afghanistan down to second, while Timor-Leste retains its third place (see Figure 7).

Figure 7. g7+ Average PEFA Comparisons (most recent PEFA)



Nb: Yemen stands out as being highly rated, though the last PEFA undertaken for that country was in 2008, and much has occurred in that country since then.

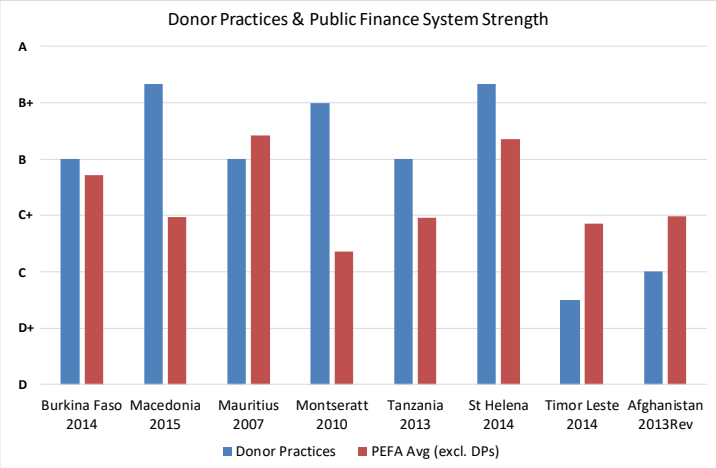
Figure 8. g7+ PEFA League Tables (most recent PEFA)

In terms of the different PEFA themes, performance is more variable. Both countries are however more consistent compared to other countries, which helps drive their overall relative good performance. Budget credibility scores for Afghanistan and Timor are in the middle of the pack, with Timor-Leste nearer the lower end. Both are way off the high-income country benchmark of "A" by Norway. Comprehensiveness and Transparency and Policy Based

Budgeting, have Afghanistan and Timor-Leste near the top of the pack with a "C+", getting close to the Norway mark of "B+". Afghanistan tops the scores for predictability and control with a high "C+", while Timor-Leste is in the middle of the pack with a high "C" – Norway is B+. Both are near the top for Accounting, Recording and Report – with Timor-Leste bettering the Norway mark. For external scrutiny they are both at the top with a high "C+" – close to the Norway mark of "B".

Afghanistan and Timor-Leste have the best donor practice scores of g7+ countries with a C and D+ respectively (see Figure 9), but the score is still well short of the best practice benchmark score of "A" delivered by the donor (UK) to St Helena, and the other ODA recipient countries that scored a "B" or better under PEFA (Burkina Faso, Macedonia, Mauritius, Montserrat, and Tanzania).

Figure 9. Best Donor Practices Comparisons (most recent PEFA)

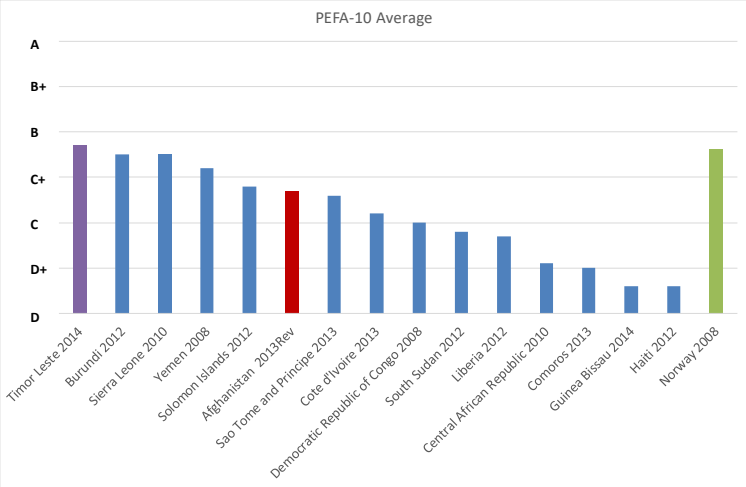


Strong systems or low fiduciary risk - appear NOT to be a dominant reason for strong donor practice. Given that both Timor-Leste and Afghanistan both have public finance systems that are rated as strong if not stronger than those aid recipient countries that do the best on Donor Practice Scores. This indicates that avoidance of systemic fiduciary risk may not be a dominating reason for poor donor practice performance as defined by the original PEFA. Perceptions, preferences and reputation risks are presumably more dominant[14]. The analysis shows that good donor practice as defined by the original 2005 PEFA is possible, though rare. The problem with accepting such an approach is that if perceptions are so bad then existing mechanisms that already bypass country systems are not working. Reports by SIGAR in Afghanistan for example indicate that bypassing country systems doesn't suddenly evaporate exposures to fiduciary risk.

What's more, claims that bypassing country systems reduces fiduciary risk exposures is on shaky ground, especially when one analyses the relative strengths of project and donor systems, and the impacts on country systems through increased fragmentation (of budgeting, accounting and scrutiny systems). We argue, that bypassing systems actually increases fiduciary risks of government systems because it increases fragmentation, adds complexity and lowers accountability all at the same time. Bypassing national systems also increases development risks as it is harder for policy makers to know how to allocate scarce resources to the most efficient and effective investment.

[14] See also analysis on the determinant of budget support in the Afghanistan Development and Fiduciary Risk Assessment 2015, which reveals that fiduciary risk is not dominant in determining levels of budget support.

Figure 10. g7+ PEFA 10 Comparisons (most recent PEFA)



In terms of PEFA-10 performance, Timor-Leste tops the g7+ countries league table with a high "C+", bettering the high-income benchmark of Norway. Afghanistan performs relatively well with a high "C" (See Figure 10).

B: g7+ Country Comparisons: Development and Fiduciary Risks

While the previous section reviewed the trends in PEFA, this sections looks at the trends in development and fiduciary risks scores. It compares results with other g7+ countries. The assessment provides an insight to the effectiveness of improving development outcomes by using country systems and targeting reforms that balance fiduciary risk reduction while increasing probabilities of securing sustainable and cost-effective development benefits.

Methodology for Quantifying Risks

Two different types of risks are distinguished: i) ***fiduciary risk***, which is defined here as essentially the short-term risk of mismanagement and misuse of funds; and ii) ***development risk***, which is the longer-term risk of not meeting development policy objectives. See Box 1 on page 9 for expanded definitions including for other risks.

This section quantifies development and fiduciary risks and builds on the PEFA quantification method used in the previous section. The approach is based on a standard risk quantification methodology adopted in other settings, including Papua New Guinea[i], Iraq[ii] & [iii], Afghanistan[iv], Turks and Caicos Islands[v], Tokelau[vi], Sri Lanka[vii], Liberia[viii], UNRWA (including West Bank and Gaza, Syria and Jordan)[ix] and Timor-Leste[x]. The approach uses a standard risk **quantification approach of: *performance score multiplied by risk factor*,** where risk factors are associated with the system generally - not the country context (see box below).

Risk Score = Score for System Performance x Risk Factor (Fiduciary or Development)

Under this approach risk factors are assigned for each performance indicator and dimension based on the assessed importance to fiduciary risk, which was defined essentially as the short-term risk of mismanagement and corruption and poor value for money[15] and applied the following numerical equivalents: High = 3, Moderate = 2 and Low = 1[16].

[15] And development risk being the longer term risk of not meeting development objectives.
[16] PEFA scores were reversed for risk quantification, where D was 4 and A was 1. This was to ensure risk scores were internally consistent. Highest risk factor matched to poorest performance score gives the highest risk score.

An important point here is that risk factors for performance indicator dimensions can be different. For example, medium term policy linked budgets are more important for longer term development risk than fiduciary risk so would get a higher development risk factor, while bank reconciliation systems are more important for short term fiduciary risk so would get a higher fiduciary risk factor. The nominal fiduciary risk score range was rebased to a 0-1 range to give more meaningful numerical values to risk levels, but importantly also enables wider use including in cost-effectiveness analysis of aid interventions and reform programs (see use in Multi-Donor Trust Fund decision analysis[xi]). Other approaches have also been adopted for rating fiduciary risk including the French Fiduciary Risk Index (FRI), which is simply a reduced PEFA set[17],[18] and [19]; the IMF PEFA Index.

Results

The Results are presented in two different ways. Countries are compared by: i) each PEFA group and theme and then ranked; and ii) individual country risk profiles using PEFA themes.

Figure 11 and Figure 12 reveal that Development risks are higher than fiduciary risks. There was a revealed and meaningful difference quantifying in fiduciary and development risks. Not only did risk scores change, but some ranks also changed when comparing development and fiduciary risks. Similar to the PEFA analysis, the results also indicate that Afghanistan and Timor-Leste do relatively well in comparison to their g7+ country peers. While the high development risk results are partially a consequence of high development risk factors, it also indicates that progress on reforms that reduce development risk are more difficult to achieve.

Reforms have indeed been difficult to secure in most countries. Examples of failures include the absence of fully functional, medium term budgets, with forward estimates that routinely roll over, systems that explain clearly the changes to baseline funding, new policy costing systems linked to medium term budgeting approaches, having consolidated budgets that are easily compared to end-of-year accounts, and complete annual reports that give both output and financial performance. These are key systems that make the budget an instrument of policy and national accountability, rather than a political rationing device or just an aggregation of ambit claims.

High-income countries are able to deliver on these basic systems. Countries like Norway, Australia, and New Zealand can do these things that make their systems resilient, accountable and transparent. There is an implicit argument that these countries only do better because they are rich. We disagree with this as reforms are not a result of their wealth, but a contributor to the country as a result of the things they do. It is the processes they follow and the nature of the culture within the institutions they have built that helps to build a sustainable public sector in these countries.

[17] The French FRI – FRI calculation is indicative. The FRI is obtained from the scores of 12 selected PEFA indicators, divided in 4 dimensions: D1 - Credibility of the budget: PI2; PI4; PI7; D2 - Effective enforcement procedures and expenditure control: PI18; PI19; PI20; D3 - Reliability of accounting and financial reporting: PI22; PI24; PI25; and D4 - Quality and external audits: PI26; PI27; PI28. [19]

[18] Bessette, 2009, "The French Doctrine on Fiduciary Risk" IMF PFM Blog (accessed 15 Nov 2009)

[19] PEFA Secretariat, 2009, "Survey of PEFA Partners' "Use of PEFA Assessments for internal processes", PEFA, Washington DC, USA. (Accessed 5 December 2009)

Figure 11. Development Risks – PEFA Selected Themes

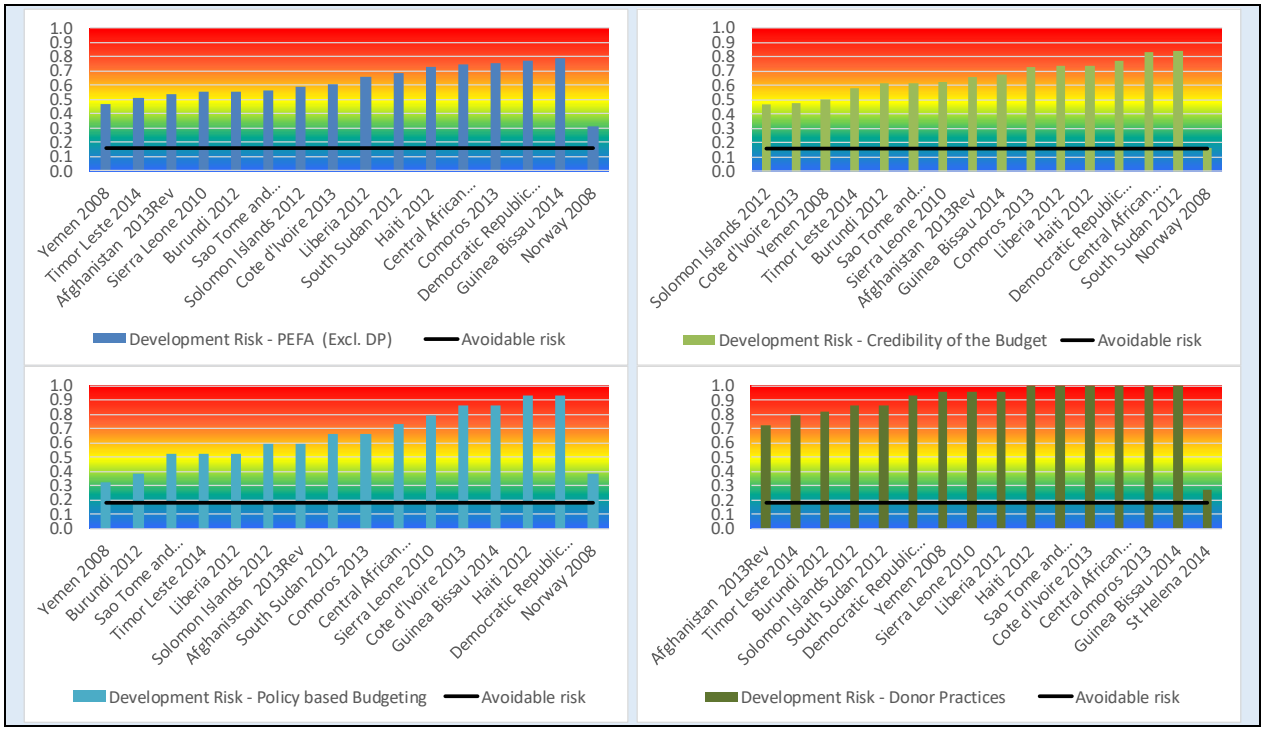
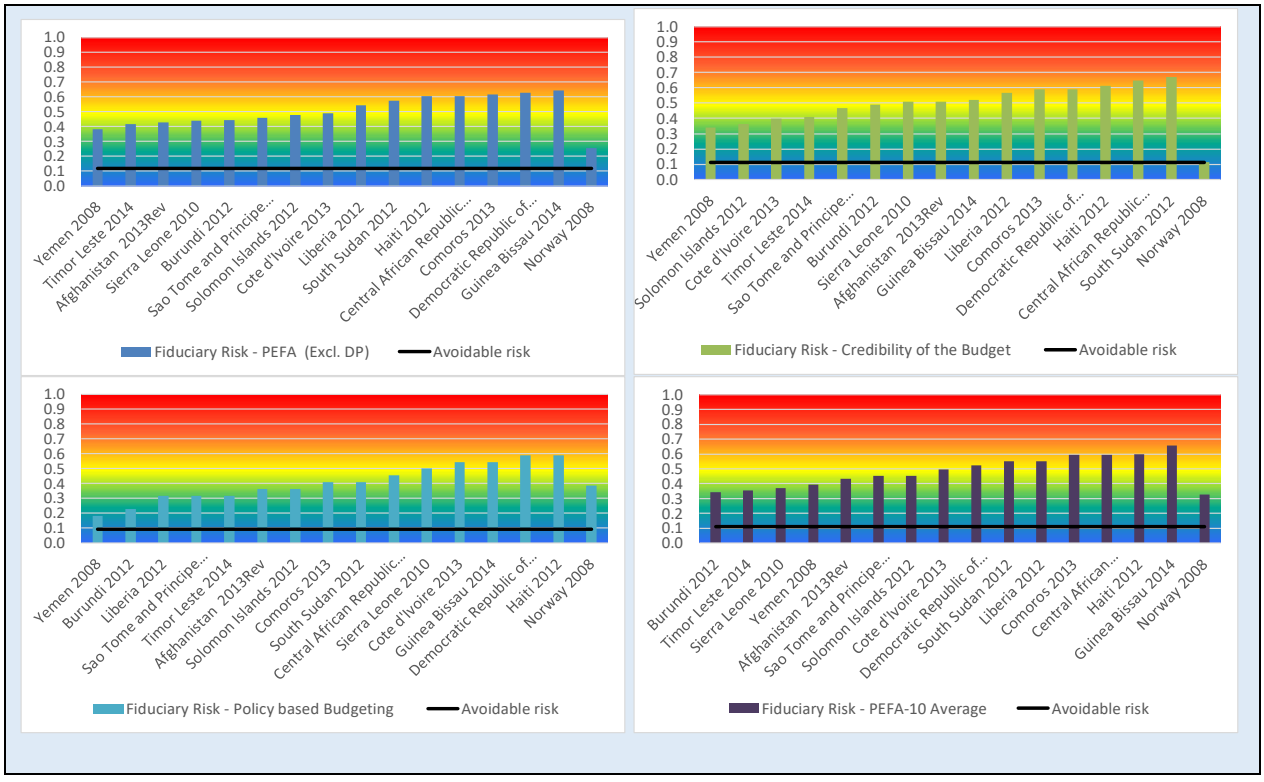


Figure 12. Fiduciary Risks – Selected PEFA Themes



C: Relative Cost-Effectiveness of Fiscal Performance Improvement Assistance in g7+ Countries

An assessment was undertaken of the value of aid money for strengthening public sector management and public finance systems in Timor-Leste, Afghanistan and other g7+ countries (those that had completed at least two (2) PEFA assessments). The standard approach to Cost-Effectiveness Analysis (CEA) was chosen as the analytical method to help determine if value for money was achieved. CEA is a type of economic evaluation technique that essentially

compares the relative costs and outputs or outcomes (effects) of at least two courses of action, such as comparing a proposed intervention with no intervention or the current prevailing intervention. CEA is different to Cost-Benefit Analysis (CBA) in that CBA assigns a monetary value to the measure of effect, whereas CEA uses a quantifiable effectiveness comparator. CEA is often used in the field of health services, where like in the development effectiveness field it is either inappropriate or too difficult to monetize effects in a useful and practical way. Using CEA methods allow us to measure the relative cost effectiveness of development assistance in delivering fiscal performance improvement, or in other words, to assess the cost effectiveness of development assistance to reduce systemic fiduciary risk.

Methodology

CEA results are expressed in terms of Cost Effectiveness Ratios (CER). CER is simply cost over effect, which can be misleading as it does not account for counterfactuals or relative performance (see equation 1 for simple average CER). In Incremental Cost Effectiveness Ratios (ICERs) (see equation 2), counterfactuals are purposely addressed: the denominator is a gain in effect $(E_1 - E_0)$ and the numerator is the cost associated with the gain in effect $(C_1 - C_0)$[20]. ICERs are generally used to compare different options, like different treatment plans in health care. A positive ICER indicates that the intervention being assessed is more effective but at a cost. Comparing ICERs among different interventions gives an indication of which intervention provides the best value or "bang for buck". Results can be ranked in terms of most expensive for a given gain. Some health systems have set ICER ceilings for the public financing of pharmaceutical drugs or health technology.

A negative ICER is difficult to interpret, since the difference in costs or difference in effects can be negative. A negative cost difference over a positive effect difference means that the intervention is cheaper and more effective. This is the 'No Brainer' choice. But a positive cost difference over a negative effect difference means that it costs more to go backwards or do worse. The magnitude of the negative ICERS is also difficult to interpret as inspection of the numerator and denominator is required.

$$\textbf{Equation 1:} \quad CER = \frac{C_t}{E_t}$$

$$\textbf{Equation 2:} \quad ICER = \frac{C_1 - C_0}{E_1 - E_0}$$

$$\textbf{Equation 3:} \quad TCER = \sum_{t=0}^{n} (DC_t - GC_t) \div \sum_{t=0}^{n} (E_t)$$

C=Costs, E=Effect, t= Time period (Year), DC = Donor Costs, GD = Government Costs.

A Timewise-Cost-Effectiveness Ratio (TCER), developed here is the sum of the annual current costs adjusted for inflation over the change in effect. The cost calculation is equivalent to the sum of the constant costs – or constant aid disbursements (see equation 3), where the effects of inflation have been excluded. Incremental costs in this case are those additional resources provided through aid – on top of non-aid or government own-source financed reform, which includes activities funded by general budget support.

[20] A commonly used outcome measure in CEA is quality-adjusted life years (QALY) as used in the field of health economics.

While it is difficult to interpret a negative ICER, it is simple to interpret negative TCERs. Under this approach it is essentially impossible to score a negative TCER from a negative numerator as aid disbursements in a particular year are almost always greater or equal to zero[21]. The negativity can only emerge from the denominator or the change in effect. So a negative TCER means that there was a cost to go backwards or do worse, implying that it may have been better to not have intervened in the first place. That said, without the counterfactual or more information on what was actually being paid for, that implication might not be valid. The idea presented here is that of "cost prevention". In other words, while the analysis may reveal a cost to go backwards, the effects without the intervention might be far costlier.

Interpreting the magnitude of a negative TCER is not so intuitive. For example, on face value, a large negative TCER may indicate a big cost to go backwards. However, a large negative TCER might actually be better than a small negative TCER: if there is only a small fraction of a deterioration, then the TCER gets big quickly due to a small number in the denominator.

Four different effectiveness measures and three different cost bases were used. The four effectiveness measures were half grade movements for:

i) simple average PEFA scores;
ii) simple average PEFA scores for the six key PEFA themes under direct control of aid recipient governments;
iii) the simple average PEFA scores excluding Donor Practices theme; and
iv) the PEFA-10 / "basics first" summary scores.

For cost of development assistance to reduce fiduciary risk, the three measures were:

i) a wide cost base;
ii) a narrow cost base; and
iii) a cost-per capita base.

The wide cost base includes all ODA reported by donors disbursed through all aid channels for the following sectors:

i) 15110: Public sector policy and administration management;
ii) 15111: Public finance management;
iii) 15112: Decentralisation and support to subnational government; and
iv) 15113: Anti-corruption organisations and institutions.

For the narrow cost base only ODA charged to 15111: Public finance management was included.

For the per capita calculations, the narrow cost base was converted to per-capita figures using population data (from the WDI database). The time-wise approach was used for quantifying different effects. Cost and effectiveness parameters were not discounted for time, though costs were set in constant terms around a 2014 base year. Parameter data and results are provided at Table 1 on page 32.

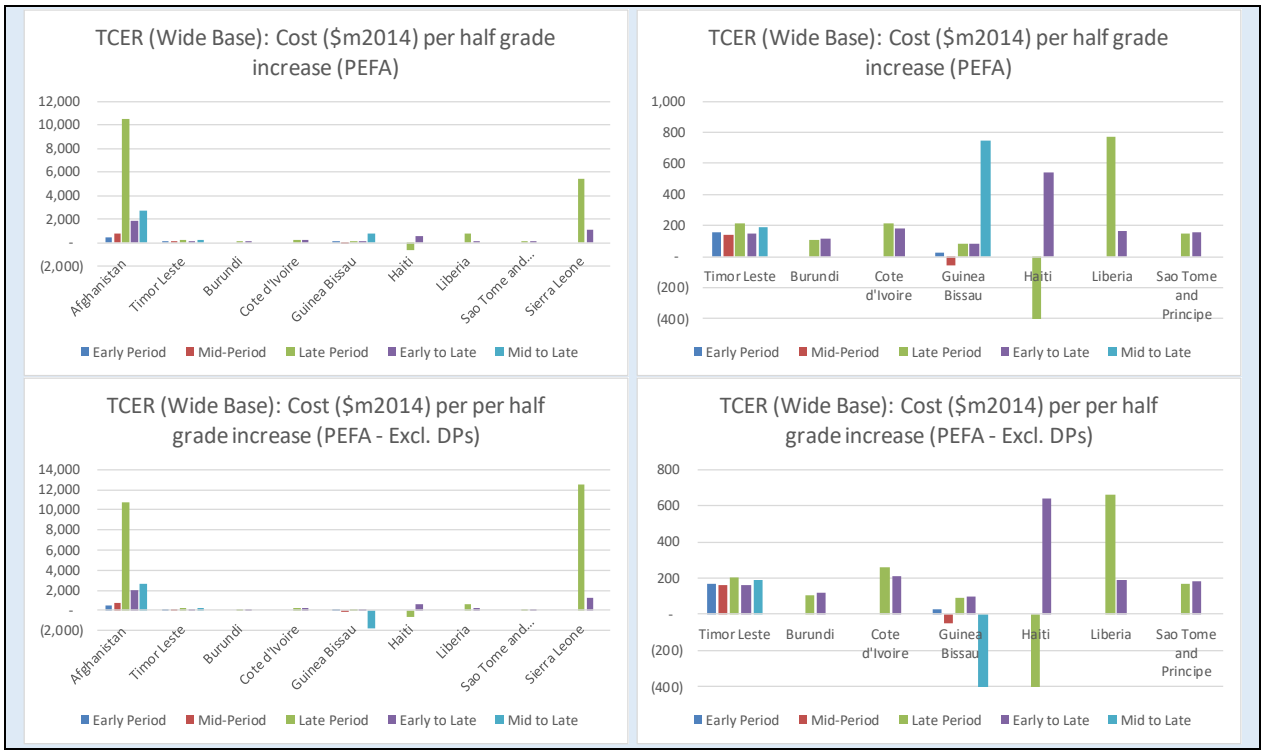
Results

The analysis reveals that Timor-Leste is much more cost-effective than Afghanistan in improving PEFA scores. Three periods were chosen for the analysis: i) the early period between around 2002 and around 2006; ii) the middle period from around 2006 to around 2010; and the late period – from around 2010 to 2015. Results are presented at Figure 13 with key parameter data and results provided in Table 1 at Attachment A: Cost-Effectiveness Data by g7+ Country.

[21] Negative aid disbursements are associated where repayments of aid are greater than new aid disbursements.

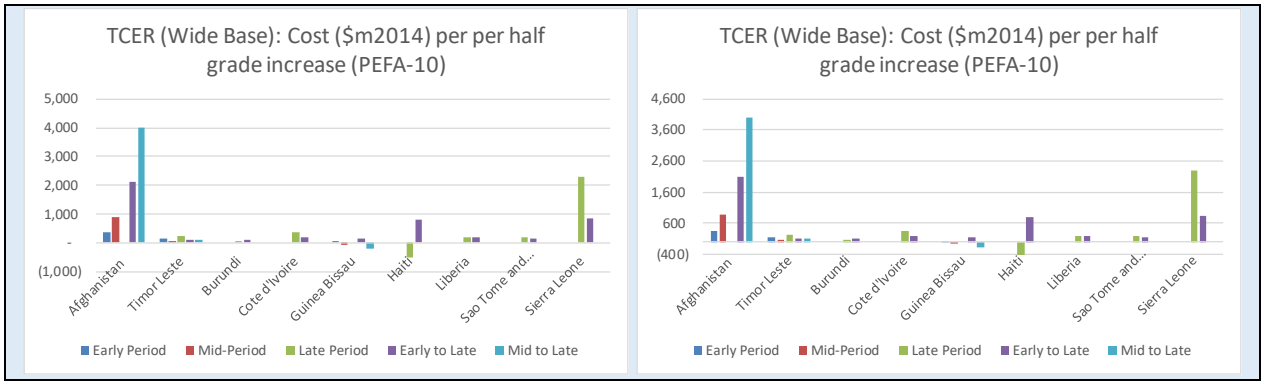
In the very early years between 2002 and 2005 Timor-Leste was around three times more cost effective (under wider and narrow cost base terms) against ICER results. Under wide cost (narrow) terms it cost donors to Timor-Leste $153.8m ($18m) to secure an average half grade improvement in the simple average PEFA score, compared to Afghanistan, which cost $496m ($50m). For comparison, another global estimate of the cost of reducing PEFA by a half grade is $50m (see Delorenzo).[22]

Figure 13. TCERs – ODA Cost (wide) Incurred to Increase PEFA Scores by half grade



For the middle period, Timor-Leste was over five times more cost effective than Afghanistan under wide cost terms and almost three times under narrow cost terms. Timor's ICER was $144m ($48m), compared to Afghanistan's $738m ($133m) under wide cost (narrow cost) terms.

Figure 14. TCERs – ODA Cost (wide) Incurred to Increase PEFA-10 Scores by half grade



[22] De le Renzo, 2009, "Taking Stock: What do PEFA Assessments tell us about PFM systems across countries?", Working Paper 302, ODI, London, UK. (Accessed 23 November 2009)

For the late period, Timor was almost fifty times more cost-effective than Afghanistan under wide cost terms and twenty-three (23) times under narrow cost terms. Timor's ICER was $214m ($42m), compared to Afghanistan's $10.5billion ($1billion) under wide cost (narrow cost) terms.

Afghanistan is an outlier when compared to other g7+ countries, other than Sierra Leone, which had similar high results in the late period. Haiti had significant negative ICERs of $0.6 billion for its late period (2008-2012), indicating that it went backwards with donor assistance: $257m was spent on Haiti, which went backwards from a "D+" (1.7) average to a "D" (1.4).

Similar results were found using PEFA-10 as the effectiveness measure (a basics first measure for fiduciary risk). ICERs under the wide cost base method for early, middle and late periods for Afghanistan were: $355m, $885m, and no score possible as no change in PEFA-10. For Timor-Leste the ICERs were: $146m, $71m and $213m.

Figure 15. TCERs – ODA Cost (narrow) Incurred to Increase PEFA Scores by half grade

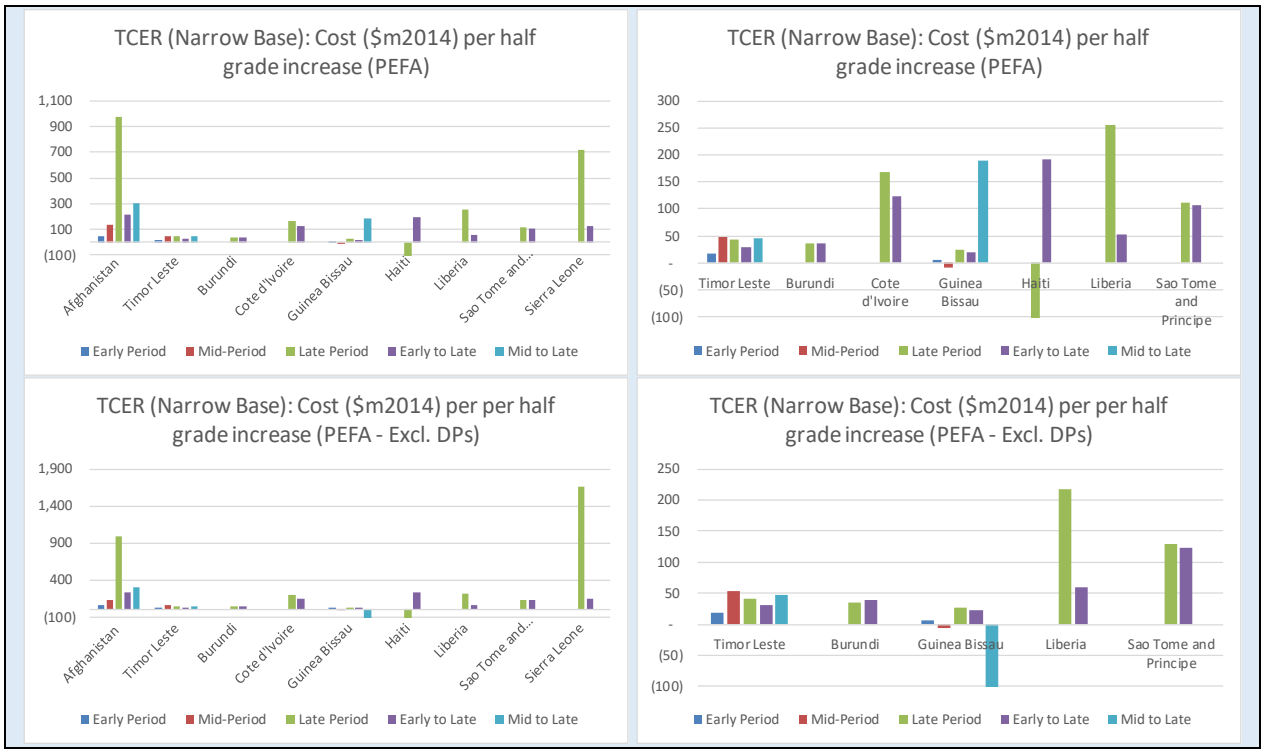


Figure 16. TCERs – ODA Cost (narrow) Incurred to Increase PEFA-10 Scores by half grade

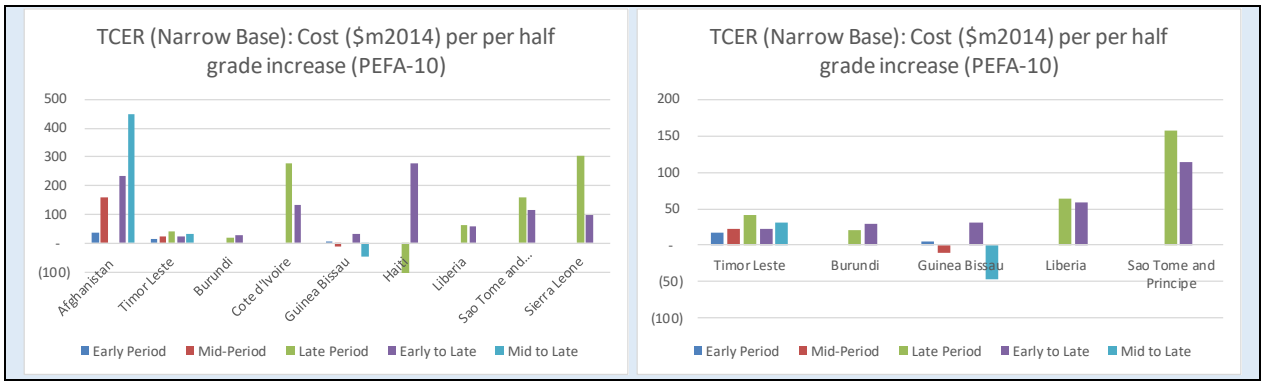


Figure 17. TCERs – ODA Cost(wide) Incurred to Increase PEFA-10 Scores by half grade

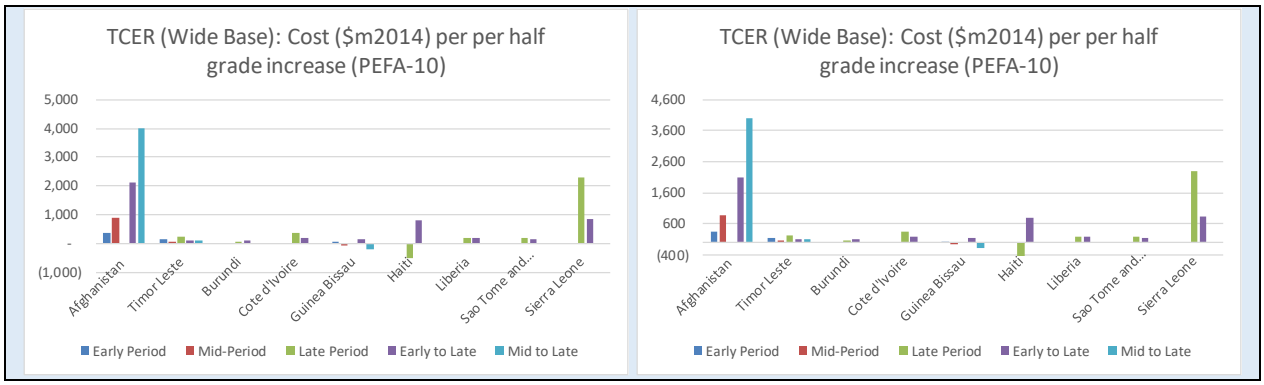
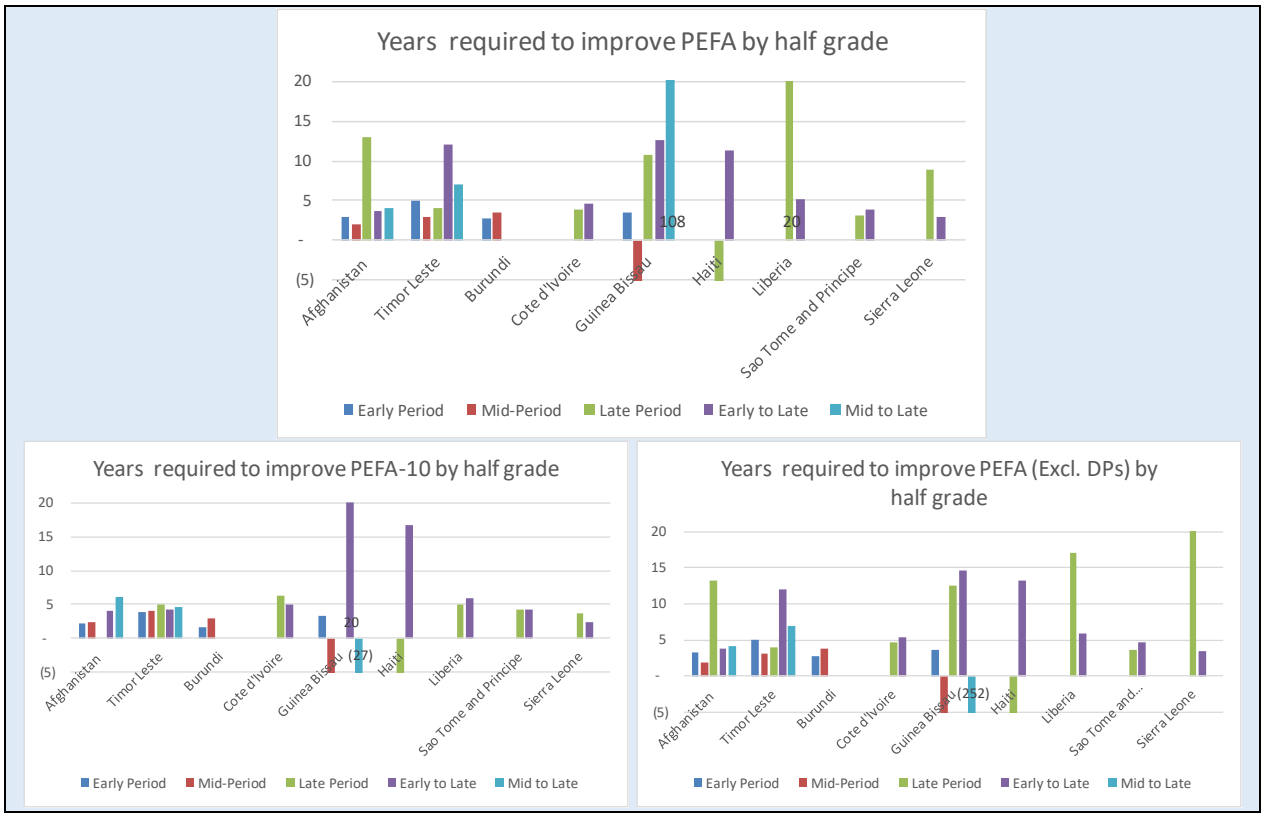


Figure 18. Years Required to Secure Half Point Grade Improvements

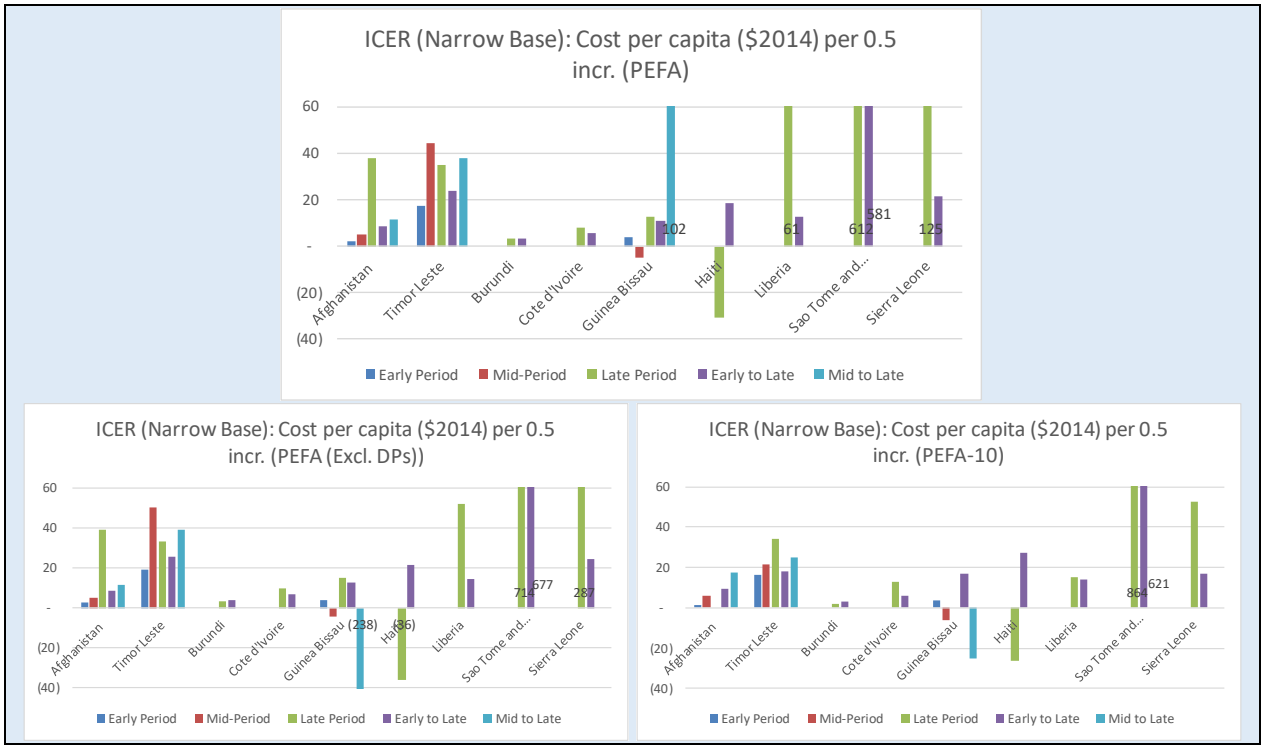


It takes on average around 3 to 5 years to increase PEFA by half a grade. This was generally the case except for Liberia, Afghanistan and Guinea in the later period (20 years, 13 years and 11 years), with Haiti going backwards in the same period. Similar results were found for reducing PEFA by a half a grade excluding Donor Practices. It was found to be quicker to reduce PEFA-10 basics first at an average rate of only 2 years.

In terms of per-capita costs, Afghanistan becomes much more cost-effective compared to Timor-Leste in the early to middle periods. In the early years it cost Afghanistan's development partners $2 per person to help raise PEFA by half a grade, where as it cost Timor-Leste's development partners $17 per person. For the middle period it was $5 compared to $45, and for the late period Timor-Leste became more cost-effective in per capita terms at $35 compared to Afghanistan's $38.

The results reveal that the early years delivered much better value for money – "much more bang for buck" – than the latter years. The result is intuitively correct, as it is theoretically easier to produce half grade quality improvements from low baselines. Three g7+ countries completed three PEFAs. All demonstrated an increased TCER in the late period compared to the early period, though Afghanistan was the most pronounced with the late period being 22 times the size of the early period. Guinea Bissau was three times bigger, while Timor-Leste was less than half (0.4) times bigger.

Figure 19. TCERs – Cost Per Capita



Other indicators of government performance reaffirm the results for Timor-Leste but not Afghanistan. Trends in IDA Resource Allocation Index results reveal that Timor-Leste came fourth out of g7+ countries, while Afghanistan came 11th, for index improvements of 0.34 compared to 0.8. The IDA Resource Allocation Index is a much wider index on government performance compared to PEFA as it covers a much broader set of policy and government systems, though it is much more opinion and perception based (See Figure 21 on page 36). Other indicators of relative performance can be found at Attachment C: Other WDI datasets" on page 36.

These results indicate that difficult reforms can be achieved cost-effectively when the conditions are right. In Afghanistan's case it has been argued that the cause for the poor result (high ICER) in the later years was a lack of focus of reform programs targeting PEFA improvements[23]. For example, a lot of effort over a long period of time had been put into Program Budgeting, even though Afghanistan was already well rated in terms of classification systems, while very little effort was put in to transforming what is arguably an auction-based budget, to one that is a policy-based budget.

In Timor-Leste's case, there have been certain conditions for a period of time that deliver difficult reforms cost-effectively. These include: i) a strong and inclusive leadership group

[23] See Afghanistan Development and Fiduciary Risk Assessment 2015

within the Ministry of Finance; ii) real ownership of reform plans; iii) credible systems to manage performance and establish the right institutional culture; iv) willing donors/development partners that share risk and support country systems. In Afghanistan's case, the same conditions are being established now. If achieved, and on the basis of this analysis, it would be expected that Afghanistan's reform efforts would accelerate resulting in stronger institutions with the right culture. The result would be reflected in improved PEFA scores over the next 3 to 5 years.

Figure 20. TCERs by PEFA Themes (narrow cost base)

D: Discussion

Working in conflict and fragile states is difficult for every well-meaning stakeholder: government officials, elected representatives, donors and contractors. This study reaffirms that view. There are various implications from this assessment, and there are methodological issues and limitations to the approach used here to understand progress, performance and value for aid money. Nevertheless, we believe there is value and a number of recommendations from this analysis are provided.

On the question of public finance system resilience - it appears to work in two ways. It can mean resistance to change for the better or worse. In other words, while it may be difficult to

build better systems, it may also be difficult to change them. People have a tendency to resist change, and routine processes are routine for a reason. This study reveals that when the conditions are right progress on reform and positive change can happen relatively quickly over a few years. Examples are Timor-Leste, once aid-dependency was broken, and Afghanistan in the early years, when there was essentially an open canvas and plenty of resources. At the same time, however, we see that when presumably the conditions are not right, progress is slow and uneven, such as in Afghanistan in the last 5 years when fragmentation increased and political will for reform reduced. Moreover, we also see that in highly difficult environments where conflict is pervasive and political settlements are tenuous, public finance system resilience can break down. We can observe that holes in systems that don't get fixed, eventually get exploited, and then protected by vested interests who wish to perpetuate financial or political gains. In particular, we have seen that donors in some countries have spent significant resources to go nowhere or even backwards against indicators of public finance system strength. Not just in Afghanistan and Sierra Leone, but other g7+ counties as well.

There is evidence that reforming weak or absent systems is easier, quicker and cheaper. The idea being that starting from a low base is much easier than working from a high base in terms of system quality. This constraint can be handled by grouping. This analysis grouped results into periods. The new 2016 PEFA framework poses some problems of ongoing trend analysis as new baselines will need to be constructed. It took seven years to pass, before this study could be contemplated. A way around this is to report during the intervening period (before reasonable trend data for the 2016 framework is available), by using a core or common and a reduced set of PEFA indicators– like the PEFA-10, or the French Fiduciary Risk Index.

This analysis of g7+ countries still reveals that reform efforts are volatile. Success over a number of years does not mean success in subsequent years. Of course this raises issues of path dependency, the importance of leadership and changes, and other factors such as the drivers of institutional culture. Further research is warranted to see if volatility in reform progress is higher in fragile and conflict-affected countries, compared to other groupings of countries.

There could well be data quality issues compromising results. PEFA is notoriously subjective, especially in the early years of its implementation. There were often debates in PEFA discussions on whether performance scores were a D or an A, let alone debates on half, grade differences. Reviewing early PEFAs with the benefit of hindsight and the backing of subsequent PEFAs, often reveals that prior scores were way off – either too generous or too harsh (which anecdotally appears to be linked to an institution or individual responsible for commissioning the analysis). The PEFA secretariat has made efforts to improve quality control via targeted training, peer reviews, and more recently, being more open and more accessible with its data. And there is evidence that PEFA assessments are becoming more robust. However, the value of trend analysis can be improved if PEFA assessments routinely look back and review past scores with the view of formally revising them in order to help build a more robust evidence base to track progress over time. And importantly report the changes in easily accessible ways. The new 2016 PEFA does appear to be less subjective in key areas, reducing discretion in scoring, such as with budget credibility where it now makes it clear than donor projects on budget are not to be excluded in calculations, which has been the case, including Afghanistan PEFAs of the past.

There are other methodology issues. Average Cost-Effectiveness Ratios (ACER), Incremental Cost-Effectiveness Ratios (ICER) and the Time-Wise Cost Effectiveness Ratios (TCER) adopted here, have their limitations. Similarly, the risk factoring approach to draw out the differences of development and fiduciary risks can reduce the reliability of results. That said, intuitively, the analysis appears to be looking in the right direction.

There are other limitations. The cost data was aggregated in only three ways. Aggregating of aid data was directed at PFM like purpose activities: i) a broad-based approach; ii) a narrow base approach; and iii) a per-capita approach. Different aggregates can be used, but the absence of more detailed data on aid purpose constrains reliability. The issue is that reported disbursements in the sector, may well not have been for fiduciary risk reduction.

The issue of value for aid money is an important one to explore further. On the face of it, this analysis shows some negative cost-effectiveness ratios that indicate that the common alternative course of action – "to do nothing" – may be better than intervening at all. Spending taxpayers' money to go nowhere or even to go backwards slowly does not appear to be good fiscal, aid or foreign policy. However, there are important considerations. The lack of counterfactuals is a key limitation. The alternative approach has not been modelled here, and nor has the consequences of no intervention. For example, financial assistance could have prevented catastrophic collapses of public finance systems that keep governments working, cities running and communities functioning. Here, we see that the limitations of the data. We don't know what the money is actually being spent on – e.g. funds may not be targeted at PFM, but on political settlements. We also have not assessed the relative methods of different development interventions.

The analysis may be masking other realities – geopolitical, aid-industry incentives and intentional misdirection. There are other interests that are in play in the aid industry, which this analysis does not address. There may be geopolitical reasons for interventions that are not clear, incentives may be in place within the aid industry that promote rather than reduce aid dependency, and/ or players that just want to steal. These problems are outside the scope of this analysis, though the issues should not be ignored.

In a way, some of the results revealed in this paper indicate that the international community may well be paying to avoid adverse effects of worse outcomes that could occur in the absence of assistance. There might well be the view that the investment is to just keep "heads above water". In other words, the cost is written off as the sunk cost to keep things from falling apart or the cost of fragility. There probably is some truth to this, however, the problem with this thinking is that it is not robust enough, and reeks of excuse making and after-the-fact justification of poor performance. The reality is more likely to be that we're not doing enough to focus efforts on the right reforms and in the right way. Nor are we focusing enough on the foundations that help institutions create cultures of high performance, and help public services and public servants be self-reliant and accountable for successes and failures.

We still have too many unanswered questions. Does using country systems to improve them in the right way deliver better results at less cost – is sector budget support better than "projectized" aid delivery? Does project-based aid actually reduce exposure to fiduciary risks or even reputation risks? Could the use of different methods of aid delivery and donor-recipient accountability frames have led to better outcomes – is performance based aid better than traditional in-kind Technical Assistance projects? Could better accountability and risk sharing between donors and recipients set better conditions for success – should a mix of fixed and variable performance payments be prioritized over traditional aid delivery systems? More research is warranted, though intuitively these questions appear to be the right ones to be asking.

This assessment did not look at the issue of absorptive capacity. Absorptive capacity is a particularly sensitive issue for g7+ countries. The problem of over aiding has been well documented by McGillivray and others. And recently, we are seeing evidence being brought

forward by the IMF[24] that over-aiding compromises a country's tax base and tax takes. Analysis in the main paper[25] reveals that Timor-Leste in the early years and Afghanistan until recently, were over aided – in different ways. The general rule of thumb for absorptive capacity limits of 20% of GDP have been breached significantly and for relatively long periods. Ministry level direct aid often breaches the 50% ceiling rule of aid to total ministry resourcing. This is an often-forgotten criterion when it comes to responsible aid giving. The theory behind it is that as soon as officials within ministries see donors rather than their minster as the source of finance, the pursuit of a desirable institutional culture breaks down. Accountability is fragmented. ***More analysis is required to drill down on the effects of bypassing country systems – budgeting, accounting and scrutiny in terms of state sovereignty and state legitimacy, as well as the informal competition between certain types of donor agencies and government for the support of a population.***

Importantly this analysis raises the point that development risk should really be much more of a concern for donors than it currently is, especially when compared to demonstrable concerns over exposure to fiduciary and reputation risks. This is not just in terms of probability, but also in terms of value for money. Not getting good development outcomes from billions in aid investments is the bigger issue than avoiding adverse domestic consequences of corruption. No donor, however, has been able to win that argument at home. A solid program of analysis of cost-effectiveness of aid interventions and development risk assessments would, however, help the case and build the evidence base. As soon as there is a concern for value for money, the link between development objectives and costs incurred in achieving them become much more important.

We believe that focusing on cost-effectiveness of aid interventions will lead to a focus on improving how aid is delivered. Focusing more on development risk can lead to different behaviours and priorities. For example, aid might be more cost effective if it is flexible: aid modalities might need to shift from project-based aid to more flexible performance orientated aid. Similarly, a focus on self-reliance and taking on the roadblocks and bottlenecks to reform, brings the idea that efforts at using country systems - budgets, accounts and audits - must be ramped up. We are still a long way from aid dependent countries having budgets that are an instrument of government policy, rather than a type of political settlement tool or just an aggregation of ambit claims or even an auction-based budget. We are also a long way off from donors not dominating the management of resource allocation in aid dependent countries, and recipient governments being primarily responsible for reporting on performance in multiple resolutions – from the aggregate to the detail.

Moving forward, this analysis indicates that there is value in analysing trends in performance including system quality and the cost-effectiveness of aid interventions in the area of public finance and national accountability. There is clearly a need to keep a value for money focus and to do better at targeting reductions in quantifiable and avoidable development and fiduciary risks. A start has been made with fiduciary and development risk data on all g7+ countries and other countries that have a published a PEFA assessment on the PEFA Secretariat website. The analysis unfortunately is not much use to governments. We have seen in other settings, that such analysis is most useful when it is done by government for government and followed-up with more foundational work of institution culture building and reducing donor induced system fragmentation and aid fragmentation more generally.

[24] See IMF Working Paper 16/12. What does aid do to fiscal policy? New Evidence.
[25] See also Development and Fiduciary Risk Assessments for Afghanistan and Timor-Leste.

The analysis reveals the importance of the "how" of development. While it is still important to make sure that what we do is in the right areas, we need to do much better on how we do it. Getting the how right, is arguably the foundation for sustainable and effective development.

ATTACHMENTS

Attachment A: Cost-Effectiveness Data by g7+ Country

Table 1. Key Cost-Effectiveness Data

Country/Measure	Data				Early Period	Mid-Period	Late Period	Early to Late	Mid to Late
Afghanistan	**2002**	**2005 Rev**	**2008 Rev**	**2013 Rev**	**2002-2005Rev**	**2005Rev-2008Rev**	**2008Rev-2013Rev**	**2002-2013Rev**	**2005Rev-2013Rev**
Cost for Period (excl. $m in PEFA yr) - Wide Base					496.3	1,149.3	4,035.9	5,681.5	5,185.2
Cost for Period (excl. $m in PEFA yr) - Narrow Base					53.0	206.9	374.0	633.9	580.9
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base					2.2	7.8	14.6	24.8	22.7
Average PEFA Grade	D	D+	C	C					
Average PEFA Score	1.0	1.5	2.3	2.5	0.5	0.8	0.2	1.5	1.0
Average PEFA Grade (Excl. DPs)	D	D	C	C					
Average PEFA Score (Excl. DPs)	1.0	1.5	2.2	2.4	0.5	0.8	0.2	1.4	1.0
PEFA 10 Grade	D	D+	C	C					
PEFA 10 Score	1.0	1.7	2.35	2.35	0.7	0.7	-	1.4	0.7
Population					24,399,948	26,528,741	25,533,217	25,533,217	25,533,217
ICER: Cost ($m) per 0.5 incr. (PEFA)					472.2	738.8	10,503.1	1,899.7	2,673.1
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))					551.0	731.4	10,705.8	1,994.1	2,661.3
ICER: Cost ($m) per 0.5 incr. (PEFA-10)					354.5	884.1	#DIV/0!	2,104.3	3,988.6
No of Years in period					3.0	3.0	5.0	11.0	8.0
Yrs req to increase PEFA by 0.5					2.9	1.9	13.0	3.7	4.1
Yrs req to increase PEFA (Excl. DPs) by 0.5					3.3	1.9	13.3	3.9	4.1
Yrs req to increase PEFA-10 by 0.5					2.1	2.3	#DIV/0!	4.1	6.2
Timor Leste	**2002**	**2007 Rev**	**2010 Rev**	**2014**	**2002-2007Rev**	**2007Rev-2010Rev**	**2010Rev-2014**	**2002-2014**	**2007Rev-2014**
Cost for Period (excl. $m in PEFA yr) - Wide Base					203.8	106.0	170.2	435.6	284.2
Cost for Period (excl. $m in PEFA yr) - Narrow Base					-	-	-	-	-
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base					22.9	32.7	27.6	67.7	57.8
Average PEFA Grade	D	D+	C	C					
Average PEFA Score	1.0	1.7	2.0	2.4	0.7	0.4	0.4	1.4	0.8
Average PEFA Grade (Excl. DPs)	D	D+	D+	C					
Average PEFA Score (Excl. DPs)	1.0	1.6	1.9	2.3	0.6	0.3	0.4	1.3	0.7
PEFA 10 Grade	D	D+	C	C+					
PEFA 10 Score	1.0	1.7	2.45	2.85	0.7	0.8	0.4	1.9	1.2
Population					1,013,194.0	1,066,409.0	1,212,107.0	1,212,107.0	1,212,107.0
ICER: Cost ($m) per 0.5 incr. (PEFA)					153.7	144.3	213.8	152.5	185.7
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))					172.1	162.2	206.2	163.6	192.2
ICER: Cost ($m) per 0.5 incr. (PEFA-10)					145.5	70.6	212.8	117.7	123.6
No of Years in period					5.0	3.0	4.0	12.0	7.0
Yrs req to increase PEFA by 0.5					3.8	4.1	5.0	4.2	4.6
Yrs req to increase PEFA (Excl. DPs) by 0.5					4.2	4.6	4.8	4.5	4.7
Yrs req to increase PEFA-10 by 0.5					3.6	2.0	5.0	3.2	3.0
Burundi	**2002**		**2009**	**2012**			**2009-2012**	**2002-2012**	
Cost for Period (excl. $m in PEFA yr) - Wide Base							116.3	319.4	
Cost for Period (excl. $m in PEFA yr) - Narrow Base							38.2	100.5	
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base							3.8	9.9	
Average PEFA Grade	D		D+	C					
Average PEFA Score	1.0		1.9	2.4			0.5	1.4	
Average PEFA Grade (Excl. DPs)	D		D+	C					
Average PEFA Score (Excl. DPs)	1.0		1.8	2.3			0.5	1.3	
PEFA 10 Grade	D		D+	C+					
PEFA 10 Score	1.0		1.80	2.75			1.0	1.8	
Population							10,124,572.0	10,124,572.0	
ICER: Cost ($m) per 0.5 incr. (PEFA)							107.3	113.1	
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))							108.5	122.3	
ICER: Cost ($m) per 0.5 incr. (PEFA-10)							61.2	91.2	
No of Years in period							3.0	10.0	
Yrs req to increase PEFA by 0.5							2.8	3.5	
Yrs req to increase PEFA (Excl. DPs) by 0.5							2.8	3.8	

Country/Measure	Data				Early Period	Mid-Period	Late Period	Early to Late	Mid to Late
Yrs req to increase PEFA-10 by 0.5							1.6	2.9	
Cote d'Ivoire	**2002**		**2008**	**2013**			**2008-2013**	**2002-2013**	
Cost for Period (excl. $m in PEFA yr) - Wide Base							279.5	429.8	
Cost for Period (excl. $m in PEFA yr) - Narrow Base							220.6	294.6	
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base							10.2	13.6	
Average PEFA Grade	D		D+	C					
Average PEFA Score	1.0		1.5	2.2			0.7	1.2	
Average PEFA Grade (Excl. DPs)	D		D	C					
Average PEFA Score (Excl. DPs)	1.0		1.5	2.0			0.5	1.0	
PEFA 10 Grade	D		D+	C					
PEFA 10 Score	1.0		1.70	2.10			0.4	1.1	
Population							21,622,490.0	21,622,490.0	
ICER: Cost ($m) per 0.5 incr. (PEFA)							212.6	178.5	
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))							259.0	208.3	
ICER: Cost ($m) per 0.5 incr. (PEFA-10)							349.4	195.3	
No of Years in period							5.0	11.0	
Yrs req to increase PEFA by 0.5							3.8	4.6	
Yrs req to increase PEFA (Excl. DPs) by 0.5							4.6	5.3	
Yrs req to increase PEFA-10 by 0.5							6.3	5.0	
Guinea Bissau	**2002**	**2006**	**2009**	**2014**	**2002-2006**	**2006-2009**	**2009-2014**	**2002-2014**	**2006-2014**
Cost for Period (excl. $m in PEFA yr) - Wide Base					21.2	20.6	37.3	79.1	55.7
Cost for Period (excl. $m in PEFA yr) - Narrow Base					4.8	3.0	11.0	18.8	14.0
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base					3.2	1.9	5.9	10.2	7.6
Average PEFA Grade	D	D	D	D					
Average PEFA Score	1.0	1.4	1.2	1.5	0.4	(0.2)	0.2	0.5	0.0
Average PEFA Grade (Excl. DPs)	D	D	D	D					
Average PEFA Score (Excl. DPs)	1.0	1.4	1.2	1.4	0.4	(0.2)	0.2	0.4	(0.0)
PEFA 10 Grade	D	D	D	D					
PEFA 10 Score	1.0	1.5	1.30	1.30	0.5	(0.2)	-	0.3	(0.2)
Population					1,494,60	1,596,832	1,844,325.0	1,844,32	1,844,325
ICER: Cost ($m) per 0.5 incr. (PEFA)					24.1	(53.0)	80.5	83.0	751.4
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))					25.0	(48.1)	94.0	96.8	(1,753.2)
ICER: Cost ($m) per 0.5 incr. (PEFA-10)					23.6	(68.7)	#DIV/0!	131.9	(185.5)
No of Years in period					3.0	3.0	5.0	12.0	8.0
Yrs req to increase PEFA by 0.5					3.4	(7.7)	10.8	12.6	108.0
Yrs req to increase PEFA (Excl. DPs) by 0.5					3.5	(7.0)	12.6	14.7	(252.0)
Yrs req to increase PEFA-10 by 0.5					3.3	(10.0)	#DIV/0!	20.0	(26.7)
Haiti	**2002**		**2008**	**2012**			**2008-2012**	**2002-2012**	
Cost for Period (excl. $m in PEFA yr) - Wide Base							256.5	480.6	
Cost for Period (excl. $m in PEFA yr) - Narrow Base							135.6	167.8	
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base							13.2	16.3	
Average PEFA Grade	D		D+	D					
Average PEFA Score	1.0		1.7	1.4			(0.2)	0.4	
Average PEFA Grade (Excl. DPs)	D		D+	D					
Average PEFA Score (Excl. DPs)	1.0		1.6	1.4			(0.2)	0.4	
PEFA 10 Grade	D		D+	D					
PEFA 10 Score	1.0		1.55	1.30			(0.3)	0.3	
Population							10,288,828.0	10,288,828.0	
ICER: Cost ($m) per 0.5 incr. (PEFA)							(595.7)	546.4	
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))							(695.0)	637.5	
ICER: Cost ($m) per 0.5 incr. (PEFA-10)							(513.0)	801.1	
No of Years in period							4.0	10.0	
Yrs req to increase PEFA by 0.5							(9.3)	11.4	
Yrs req to increase PEFA (Excl. DPs) by 0.5							(10.8)	13.3	
Yrs req to increase PEFA-10 by 0.5							(8.0)	16.7	
Liberia	**2002**		**2009**	**2012**			**2009-2012**	**2002-2012**	
Cost for Period (excl. $m in PEFA yr) - Wide Base							116.3	319.4	

Country/Measure	Data			Early Period	Mid-Period	Late Period	Early to Late	Mid to Late
Cost for Period (excl. $m in PEFA yr) - Narrow Base						38.2	100.5	
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base						9.1	24.0	
Average PEFA Grade	D	D+	D+					
Average PEFA Score	1.0	1.9	2.0			0.1	1.0	
Average PEFA Grade (Excl. DPs)	D	D+	D+					
Average PEFA Score (Excl. DPs)	1.0	1.8	1.8			0.1	0.8	
PEFA 10 Grade	D	D+	D+					
PEFA 10 Score	1.0	1.55	1.85			0.3	0.9	
Population						4,190,155.0	4,190,155.0	
ICER: Cost ($m) per 0.5 incr. (PEFA)						775.3	167.5	
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))						660.0	189.9	
ICER: Cost ($m) per 0.5 incr. (PEFA-10)						193.8	187.9	
No of Years in period						3.0	10.0	
Yrs req to increase PEFA by 0.5						20.0	5.2	
Yrs req to increase PEFA (Excl. DPs) by 0.5						17.0	5.9	
Yrs req to increase PEFA-10 by 0.5						5.0	5.9	
Sao Tome and Principe	**2002**	**2007**	**2013**			**2007-2013**	**2002-2013**	
Cost for Period (excl. $m in PEFA yr) - Wide Base						287.1	429.8	
Cost for Period (excl. $m in PEFA yr) - Narrow Base						220.6	294.6	
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base						1,209.4	1,615.4	
Average PEFA Grade	D	D	C					
Average PEFA Score	1.0	1.4	2.4			1.0	1.4	
Average PEFA Grade (Excl. DPs)	D	D	C					
Average PEFA Score (Excl. DPs)	1.0	1.3	2.2			0.8	1.2	
PEFA 10 Grade	D	D+	C					
PEFA 10 Score	1.0	1.60	2.30			0.7	1.3	
Population						182,386.0	182,386.0	
ICER: Cost ($m) per 0.5 incr. (PEFA)						145.2	154.5	
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))						169.4	180.2	
ICER: Cost ($m) per 0.5 incr. (PEFA-10)						205.1	165.3	
No of Years in period						6.0	11.0	
Yrs req to increase PEFA by 0.5						3.0	4.0	
Yrs req to increase PEFA (Excl. DPs) by 0.5						3.5	4.6	
Yrs req to increase PEFA-10 by 0.5						4.3	4.2	
Sierra Leone	**2002**	**2007**	**2010**			**2007-2010**	**2002-2010**	
Cost for Period (excl. $m in PEFA yr) - Wide Base						1,833.2	2,956.9	
Cost for Period (excl. $m in PEFA yr) - Narrow Base						243.4	337.3	
Cost per capita for Period (excl. $ in PEFA yr) - Narrow Base						42.1	58.4	
Average PEFA Grade	D	C	C					
Average PEFA Score	1.0	2.2	2.4			0.2	1.4	
Average PEFA Grade (Excl. DPs)	D	C	C					
Average PEFA Score (Excl. DPs)	1.0	2.1	2.2			0.1	1.2	
PEFA 10 Grade	D	C	C+					
PEFA 10 Score	1.0	2.35	2.75			0.4	1.8	
Population						5,775,902.0	5,775,902.0	
ICER: Cost ($m) per 0.5 incr. (PEFA)						5,424.2	1,088.1	
ICER: Cost ($m) per 0.5 incr. (PEFA (Excl. DPs))						12,485.5	1,244.0	
ICER: Cost ($m) per 0.5 incr. (PEFA-10)						2,291.5	844.8	
No of Years in period						3.0	8.0	
Yrs req to increase PEFA by 0.5						8.9	2.9	
Yrs req to increase PEFA (Excl. DPs) by 0.5						20.4	3.4	
Yrs req to increase PEFA-10 by 0.5						3.8	2.3	

Attachment B: Development and Fiduciary Risk Data by g7+ Country

Table 2. Development Risks by g7+ Country

Country Year	PEFA (No. DP)	PEFA	Budget Credibility	Transparency	Policy based Budgets	Predictability	Accounting	Scrutiny	Donor Practice	PEFA-10
Afghanistan 2013Rev	0.80	0.82	0.86	0.87	0.86	0.80	0.69	0.73	0.91	0.81
Burundi 2012	0.82	0.83	0.82	0.87	0.80	0.83	0.63	0.95	0.94	0.76
Central African Republic 2010	0.90	0.92	0.92	0.91	0.91	0.86	0.88	0.94	1.00	0.91
Comoros 2013	0.91	0.92	0.89	0.94	0.89	0.91	0.88	0.94	1.00	0.91
Cote d'Ivoire 2013	0.83	0.86	0.77	0.87	0.95	0.79	0.74	0.88	1.00	0.83
Democratic Republic of Congo 2008	0.88	0.90	0.84	0.92	0.98	0.94	0.74	0.86	0.98	0.84
Guinea Bissau 2014	0.92	0.93	0.81	0.97	0.95	0.90	0.90	0.97	1.00	0.94
Haiti 2012	0.93	0.94	0.92	0.95	0.98	0.92	0.91	0.88	1.00	0.94
Liberia 2012	0.87	0.89	0.92	0.92	0.84	0.84	0.85	0.86	0.98	0.88
Norway 2008	0.7	0.7	0.6	0.8	0.8	0.7	0.6	0.7	0.0	0.6
Sao Tome and Principe 2013	0.81	0.84	0.82	0.83	0.84	0.82	0.80	0.79	1.00	0.83
Sierra Leone 2010	0.81	0.84	0.85	0.84	0.93	0.84	0.58	0.83	0.98	0.75
Solomon Islands 2012	0.85	0.86	0.90	0.85	0.86	0.85	0.70	0.92	0.95	0.80
South Sudan 2012	0.89	0.90	0.95	0.89	0.89	0.92	0.81	0.86	0.95	0.86
St Helena 2014	0.7	0.7	0.7	0.9	0.8	0.8	0.6	0.6	0.8	0.8
Timor Leste 2014	0.80	0.82	0.88	0.86	0.84	0.87	0.64	0.73	0.93	0.75
Yemen 2008	0.80	0.83	0.82	0.82	0.77	0.86	0.74	0.79	0.98	0.80
Best Possible	0.63	0.65	0.64	0.73	0.73	0.65	0.45	0.61	0.73	0.62

Table 3. Fiduciary Risks by g7+ Country

Country Year	PEFA (No. DP)	PEFA	Budget Credibility	Transparency	Policy based Budgets	Predictability	Accounting	Scrutiny	Donor Practice	PEFA-10
Afghanistan 2013Rev	0.70	0.71	0.78	0.81	0.64	0.82	0.69	0.47	0.73	0.71
Burundi 2012	0.72	0.73	0.72	0.78	0.50	0.85	0.63	0.85	0.79	0.66
Central African Republic 2010	0.84	0.85	0.88	0.85	0.73	0.89	0.88	0.83	0.91	0.84
Comoros 2013	0.84	0.85	0.80	0.91	0.68	0.93	0.88	0.83	0.91	0.86
Cote d'Ivoire 2013	0.75	0.77	0.63	0.78	0.82	0.81	0.74	0.71	0.91	0.74
Democratic Republic of Congo 2008	0.82	0.82	0.80	0.83	0.86	0.96	0.74	0.71	0.86	0.75
Guinea Bissau 2014	0.86	0.86	0.73	0.91	0.82	0.91	0.90	0.88	0.91	0.87
Haiti 2012	0.86	0.87	0.82	0.89	0.86	0.93	0.91	0.74	0.91	0.87
Liberia 2012	0.78	0.79	0.86	0.81	0.59	0.85	0.85	0.71	0.88	0.78
Norway 2008	0.56	0.56	0.45	0.66	0.50	0.73	0.64	0.41	0.00	0.52
Sao Tome and Principe 2013	0.71	0.74	0.74	0.70	0.59	0.84	0.80	0.59	0.91	0.71
Sierra Leone 2010	0.72	0.74	0.74	0.72	0.77	0.85	0.58	0.65	0.88	0.63
Solomon Islands 2012	0.75	0.76	0.77	0.73	0.64	0.88	0.70	0.80	0.82	0.67
South Sudan 2012	0.81	0.81	0.90	0.80	0.68	0.93	0.81	0.71	0.82	0.76
St Helena 2014	0.59	0.57	0.52	0.85	0.45	0.80	0.64	0.30	0.42	0.65
Timor Leste 2014	0.69	0.70	0.82	0.72	0.59	0.88	0.64	0.47	0.77	0.61
Yemen 2008	0.68	0.71	0.75	0.70	0.45	0.87	0.74	0.56	0.88	0.66
Best Possible	0.47	0.45	0.45	0.61	0.36	0.69	0.45	0.24	0.36	0.44

Attachment C: Other WDI datasets for g7+ Countries

Figure 21. g7+ IDA Resource Allocation Index Trends

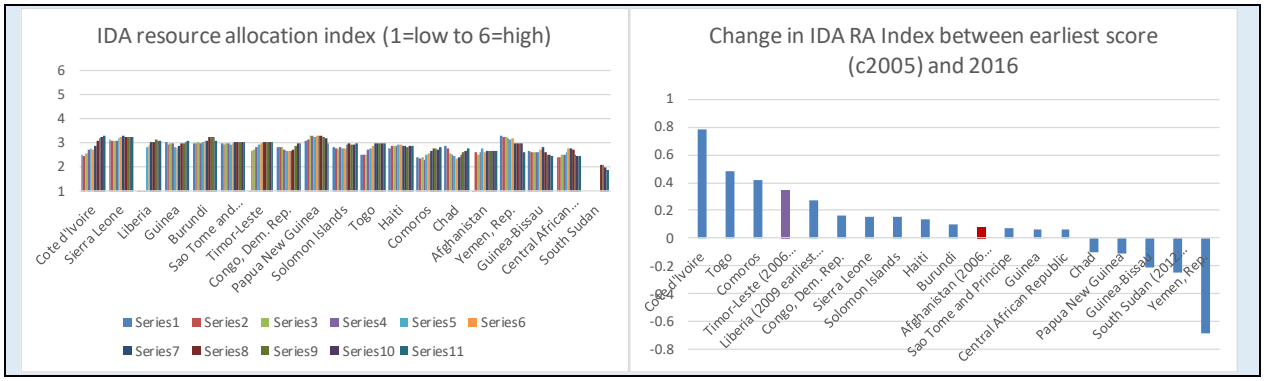
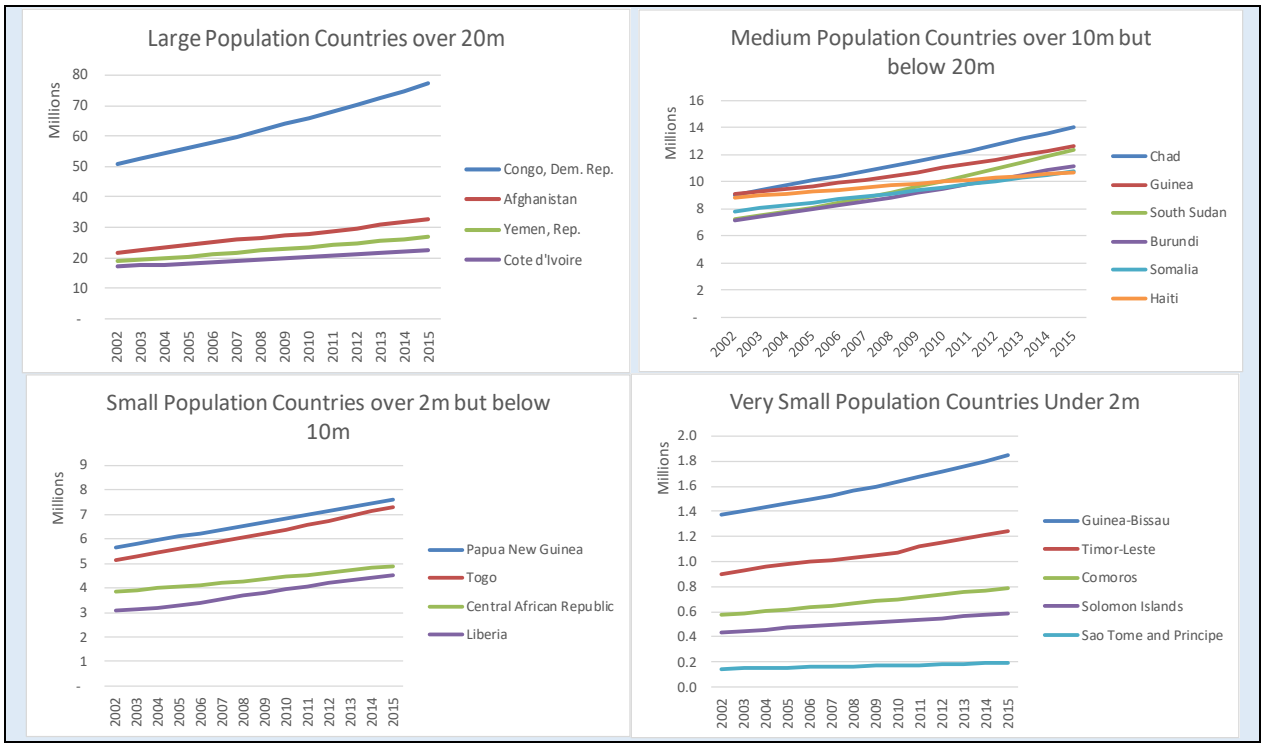


Figure 22. g7+ Country Populations



Institute for State Effectiveness

Figure 23. g7+ Country Economies

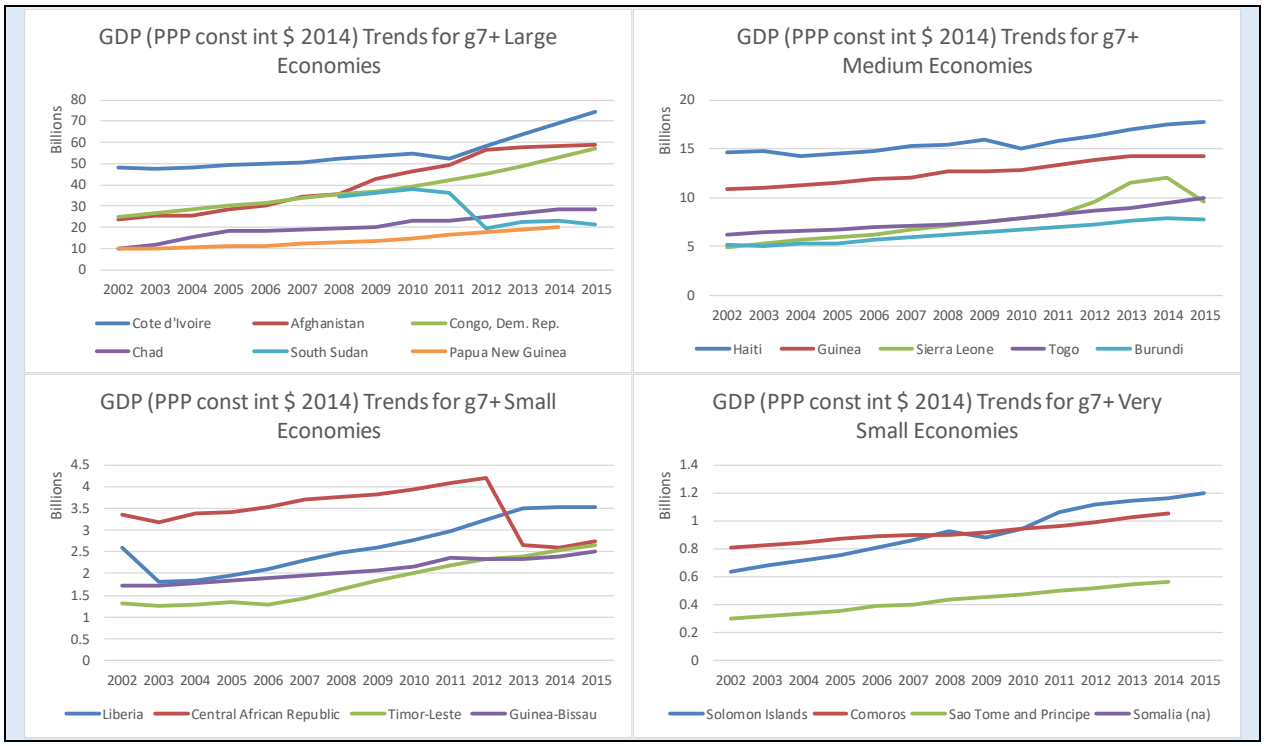


Figure 24. g7+ Country Wealth

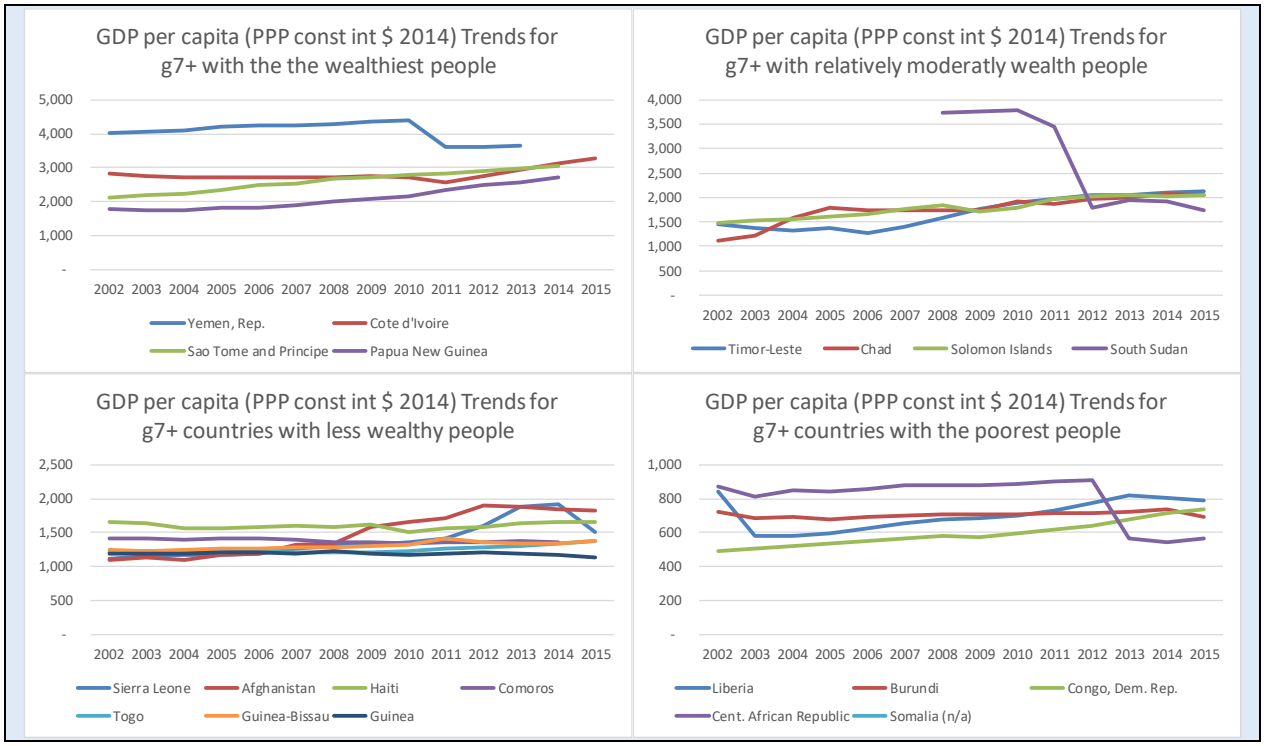


Figure 25. g7+ Country Infant Mortality Rates

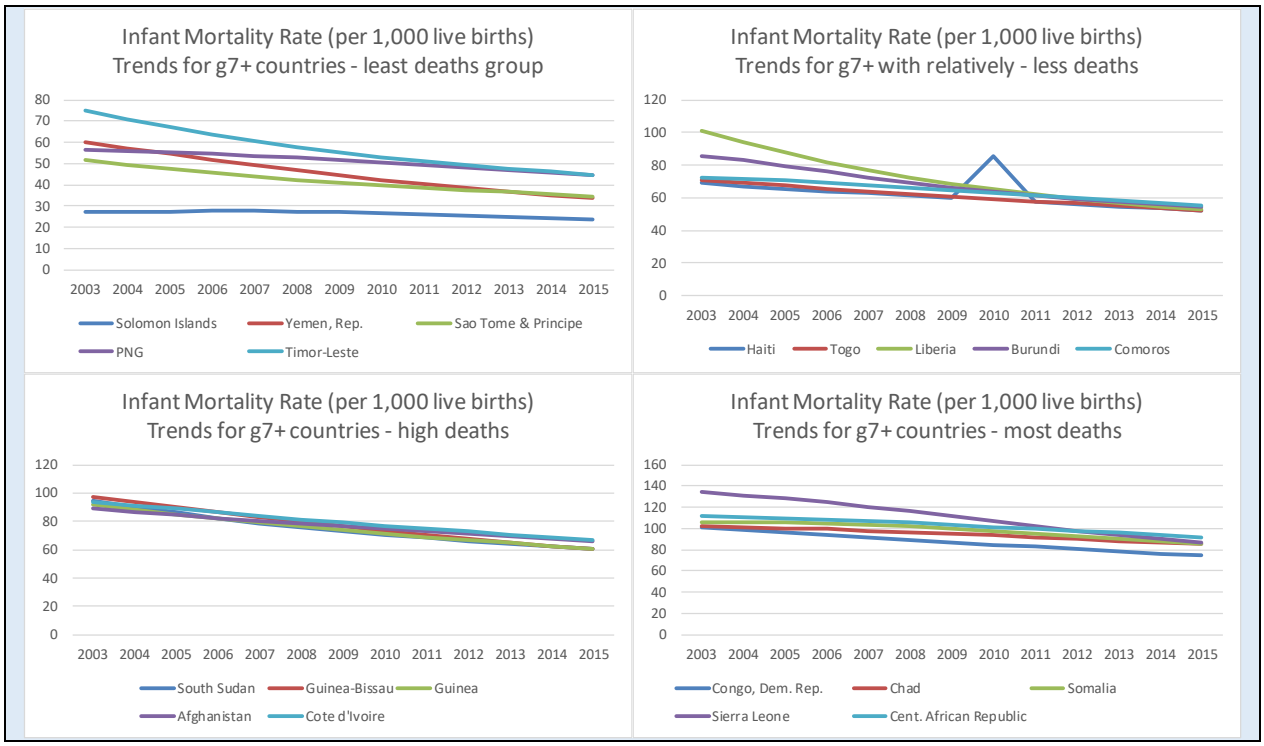


Figure 26. g7+ Country Female Secondary School Enrollment

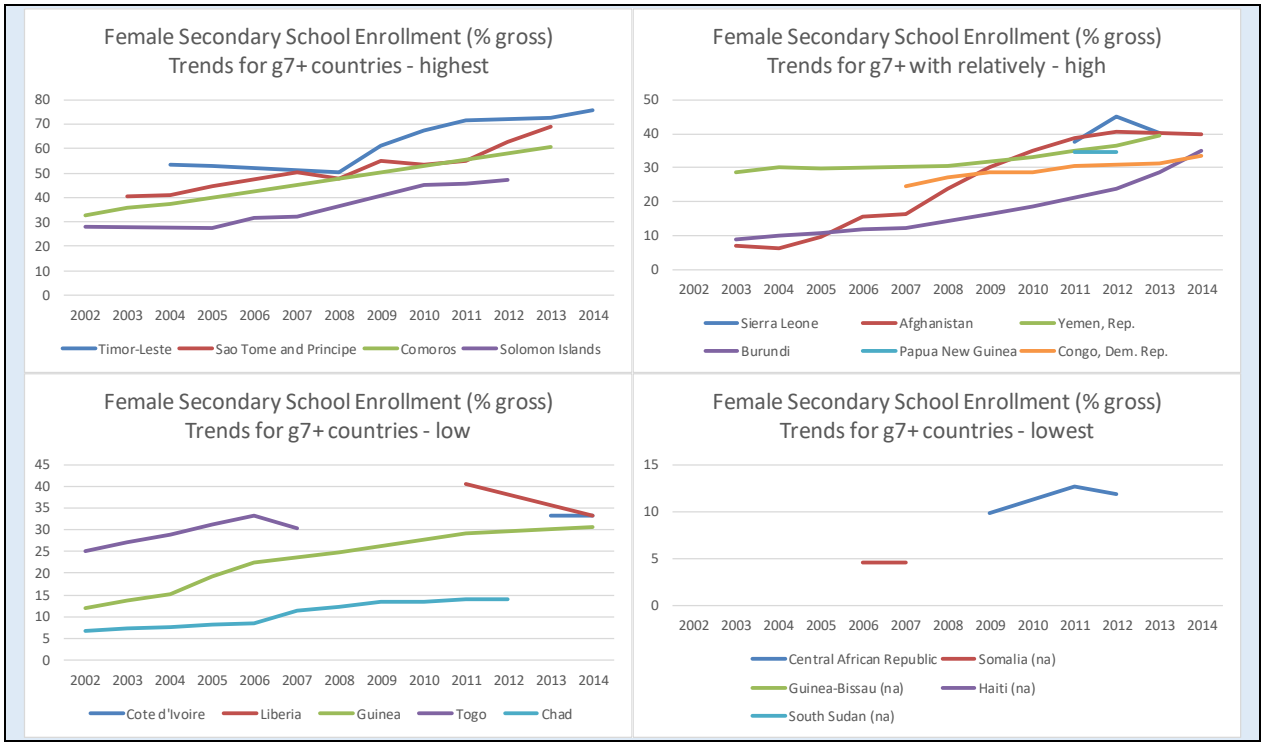


Table 4. Development and Fiduciary Risk Factors

NB: Yellow shaded cells highlight where a development risk factor is different to the fiduciary risk factor.

#	Indicator	FR Factor	DR Factor
	A. PFM-OUT-TURNS: Credibility of the budget		
PI-1	**Aggregate [sector] expenditure out-turn compared to original approved budget**	**M**	**H**
	(i) The difference between actual primary [sector] expenditure and the originally budgeted primary expenditure (i.e. excluding debt service charges, but also excluding externally financed project expenditure).	M	H
PI-2	**Composition of [sector] expenditure out-turn compared to original approved budget**	**M**	**H**
	(i) Extent to which variance in primary [sector] expenditure composition exceeded overall deviation in primary expenditure (as defined in PI-1) during the last three years.	M	H
PI-3	**Aggregate [sector specific non-tax] revenue out-turn compared to original approved budget**	**M**	**M**
	(i) Actual domestic [sector specific non-tax] revenue collection compared to domestic revenue estimates in the original, approved budget.	M	M
PI-4	**Stock and monitoring of [sector] expenditure payment arrears**	**H**	**H**
	(i) Stock of expenditure payment arrears [in the sector] (as a % of actual total expenditure for the corresponding fiscal year) & any recent change in the stock.	H	H
	(ii) Availability of data for monitoring the stock of expenditure payment arrears [in the sector]	H	H
	B. KEY CROSS-CUTTING ISSUES: Comprehensiveness and Transparency		
PI-5	**Classification of the budget [in the sector]**	**L**	**H**
	(i) The classification system used for formulation, execution and reporting of the central {SN} government's budget [for the sector].	L	H
PI-6	**Comprehensiveness of information included in budget documentation**	**L**	**H**
	(i) Share of the listed information in the budget documentation most recently issued by the central {SN} government	L	H
PI-7	**Extent of unreported government operations [in the sector]**	**H**	**H**
	(i) The level of extra-budgetary expenditure (other than donor funded projects) which is unreported i.e. not included in [sector] fiscal reports.	H	H
	(ii) Income /expenditure information on donor-funded projects which is included in [sector] fiscal reports.	H	H
PI-8	**Transparency of inter-governmental fiscal relations [within the sector]**	**H**	**H**
	(i) Transparent and rules based systems in the horizontal [sub-sector] allocation among SN governments [institutions] of unconditional and conditional transfers from central {higher level SN} government (both budgeted and actual allocations);	H	H
	(ii) Timeliness of reliable information to {lower level} SN governments [sector institutions] on their allocations from central government for the coming year;	H	H
	(iii) Extent to which consolidated fiscal data (at least on revenue and expenditure) is collected and reported for general government according to sectoral [sub-sectoral] categories. {Extent to which financial information (at least on revenue and expenditure) is collected and reported by SN government according to sectoral categories.}	H	H
PI-9	**Oversight of aggregate fiscal risk from other public sector entities**	**H**	**H**
	(i) Extent of central {SN} government monitoring of AGAs and PEs.	H	H
	(ii) Extent of central {SN} government monitoring of [lower level} SN government's fiscal position	H	H
PI-10	**Public access to key [sector specific] fiscal information**	**H**	**H**
	(i) Number of the listed elements of public access to information that is fulfilled	H	H
	C. BUDGET CYCLE		
	C (i) Policy based Budgeting		
PI-11	**Orderliness and participation in the annual budget process [within the sector]**	**M**	**H**
	(i) Existence of and adherence to a fixed budget calendar [consistency of the sector's calendar with that of the Ministry of Finance];	M	H
	(ii) Clarity/ comprehensiveness of and political involvement [involvement of sub-sector units] in the guidance on the preparation of budget submissions (budget circular or equivalent);	M	H
	(iii) Timely budget approval by the [sector committee in the] legislature or similarly mandated body (within the last three years);	M	H
PI-12	**Multi-year perspective in [sector] fiscal planning, expenditure policy and budgeting**	**M**	**H**
	(i) Preparation of multi -year fiscal forecasts and functional [sub-functional] allocations	M	H
	(ii) Scope and frequency of debt sustainability analysis	H	H
	(iii) Existence of [detailed] sector strategies with multi-year costing of recurrent and investment expenditure [for sub-sector units and programs];	M	H
	(iv) Linkages between [sector] investment budgets and forward expenditure estimates.	M	H
	C (ii) Predictability and Control in Budget Execution		
PI-13	**Transparency of taxpayer obligations and liabilities**	**H**	**H**
	(i) Clarity and comprehensiveness of tax liabilities	H	H
	(ii) Taxpayer access to information on tax liabilities and administrative procedures.	H	H
	(iii) Existence and functioning of a tax appeals mechanism.	H	H

#	Indicator	FR Factor	DR Factor
PI-14	**Effectiveness of measures for taxpayer registration and tax assessment**	**M**	**M**
	(i) Controls in the taxpayer registration system.	M	M
	(ii) Effectiveness of penalties for non-compliance with registration and declaration obligations	M	M
	(iii) Planning and monitoring of tax audit and fraud investigation programs.	H	M
PI-15	**Effectiveness in collection of tax payments**	**H**	**H**
	(i) Collection ratio for gross tax arrears, being the percentage of tax arrears at the beginning of a fiscal year, which was collected during that fiscal year (average of the last two fiscal years).	H	M
	(ii) Effectiveness of transfer of tax collections to the Treasury by the revenue administration.	H	M
	(iii) Frequency of complete accounts reconciliation between tax assessments, collections, arrears records and receipts by the Treasury.	H	M
PI-16	**Predictability in the availability of funds for commitment of expenditures [in the sector]**	**H**	**H**
	(i) Extent to which [sector] cash flows are forecast and monitored	H	H
	(ii) Reliability and horizon of periodic in-year information to MDAs [in the sector] on ceilings for expenditure commitment	H	H
	(iii) Frequency and transparency of adjustments to [sector] budget allocations, which are decided above the level of management of [sub-sector] MDAs	H	H
PI-17	**Recording and management of cash balances, debt and guarantees [in the sector]**	**H**	**H**
	(i) Quality of debt data recording and reporting [in the sector]	H	H
	(ii) Extent of consolidation of the government's [sector] cash balances	H	H
	(iii) Systems for contracting loans and issuance of guarantees [in the sector].	H	H
PI-18	**Effectiveness of [sector] payroll controls**	**H**	**H**
	(i) Degree of integration and reconciliation between personnel records and payroll data [in the sector].	H	H
	(ii) Timeliness of changes to personnel records and the payroll [in the sector]	H	H
	(iii) Internal controls of changes to personnel records and the payroll [in the sector]	H	H
	(iv) Existence of payroll audits to identify control weaknesses and/or ghost workers [in the sector]	H	H
PI-19	**Competition, value for money and controls in procurement [in the sector]**	**H**	**H**
	(i) Evidence on the use of open competition for award of contracts [in the sector]	H	H
	(ii) Extent of justification for use of less competitive procurement methods [in the sector]	H	H
	(iii) Existence and operation of a procurement complaints mechanism	H	H
PI-20	**Effectiveness of internal controls for non-salary expenditure [within the sector]**	**H**	**H**
	(i) Effectiveness of expenditure commitment controls [within the sector]	H	H
	(ii) Comprehensiveness, relevance and understanding of other internal control rules/ procedures [within the sector]	H	H
	(iii) Degree of compliance with rules for processing and recording transactions [within the sector]	H	H
PI-21	**Effectiveness of internal audit [within the sector]**	**H**	**M**
	(i) Coverage and quality of the internal audit function [within the sector]	H	M
	(ii) Frequency and distribution of reports [within the sector]	H	M
	(iii) Extent of management response to internal audit findings [within the sector]	H	H
	C (iii) Accounting, Recording and Reporting		
PI-22	**Timeliness and regularity of accounts reconciliation [within the sector]**	**H**	**H**
	(i) Regularity of bank reconciliations [within the sector]	H	H
	(ii) Regularity of reconciliation and clearance of suspense accounts and advances [within the sector]	H	H
PI-23	**Availability [Collection and processing] of information on resources received by service delivery units [in the sector]**	**H**	**H**
	(i) Collection and processing of information to demonstrate the resources that were actually received (in cash and kind) by the most common front-line service delivery units (focus on primary schools and primary health clinics) in relation to the overall resources made available to the sector(s), irrespective of which level of government is responsible for the operation and funding of those units.	H	H
PI-24	**Quality and timeliness of in-year [sector] budget reports**	**L**	**L**
	(i) Scope of [sector] reports in terms of coverage and compatibility with budget estimates	L	L
	(ii) Timeliness of the issue of [sector] reports	L	L
	(iii) Quality of [sectoral] information	L	L
PI-25	**Quality and timeliness of annual [sector] financial statements**	**M**	**M**
	(i) Completeness of the [sector] financial statements	M	M
	(ii) Timeliness of submission of the [sector] financial statements	M	M
	(iii) Accounting standards used [in the sector]	M	M
	C (iv) External Scrutiny and Audit		
PI-26	**Scope, nature and follow-up of external audit**	**M**	**H**
	(i) Scope/nature of audit performed (incl. adherence to auditing standards) [in the sector]	M	H
	(ii) Timeliness of submission of [sector] audit reports to legislature.	M	M
	(iii) Evidence of follow up on [sector] audit recommendations.	H	H
PI-27	**Legislative scrutiny of the annual budget law [by sector committees where applicable]**	**L**	**M**
	(i) Scope of the legislature's scrutiny [of the sector}	L	L

#	Indicator	FR Factor	DR Factor
	(ii) Extent to which the legislature's [sectoral committee] procedures are well-established and respected	L	M
	(iii) Adequacy of time for the legislature to provide a response to [sector] budget proposals	L	M
	(iv) Rules for in-year amendments to the [sector] budget without ex-ante approval by the legislature	L	L
PI-28	**Legislative scrutiny of external audit reports [relating to the sector]**	**M**	**H**
	(i) Timeliness of examination of [sector] audit reports by the legislature (for reports received within the last three years).	M	H
	(ii) Extent of hearings on key findings [relating to the sector] undertaken by the legislature.	M	H
	(iii) Issuance of recommended actions by the legislature and implementation by the [sector] executive.	M	H
	D. DONOR PRACTICES		
D-1	**Predictability of Direct [sector] Budget Support**	**M**	**H**
	(i) Annual deviation of actual [sector] budget support from the forecast provided by the donor agencies at least six weeks prior to the government submitting its budget proposals to the legislature (or equivalent approving body).	M	H
	(ii) In-year timeliness of donor disbursements (compliance with aggregate quarterly estimates) [for the sector]	M	H
D-2	**Financial information [for the sector] provided by donors for budgeting and reporting on project and program aid**	**M**	**H**
	(i) Completeness and timeliness of budget estimates [for the sector] by donors for project support.	M	H
	(ii) Frequency and coverage of reporting [for the sector] by donors on actual donor flows for project support.	M	H
D-3	**Proportion of aid that is managed by use of national procedures**	**M**	**H**
	(i) Overall proportion of aid funds to central government that are managed through national procedures (procurement, payment/ accounting, audit and reporting)	M	H

Figure 27. Development Risks – PEFA Themes

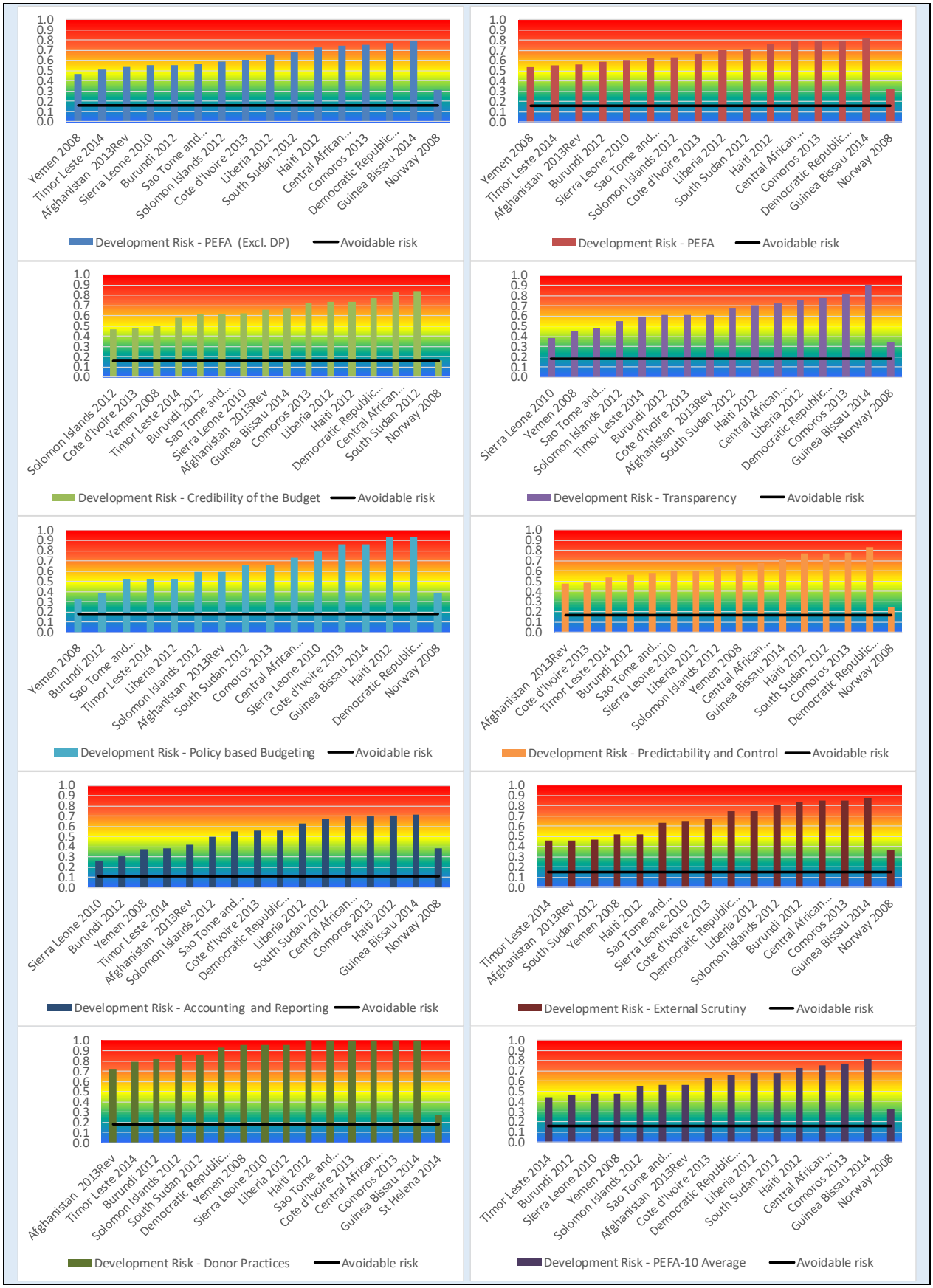


Figure 28. Fiduciary Risks – PEFA Themes

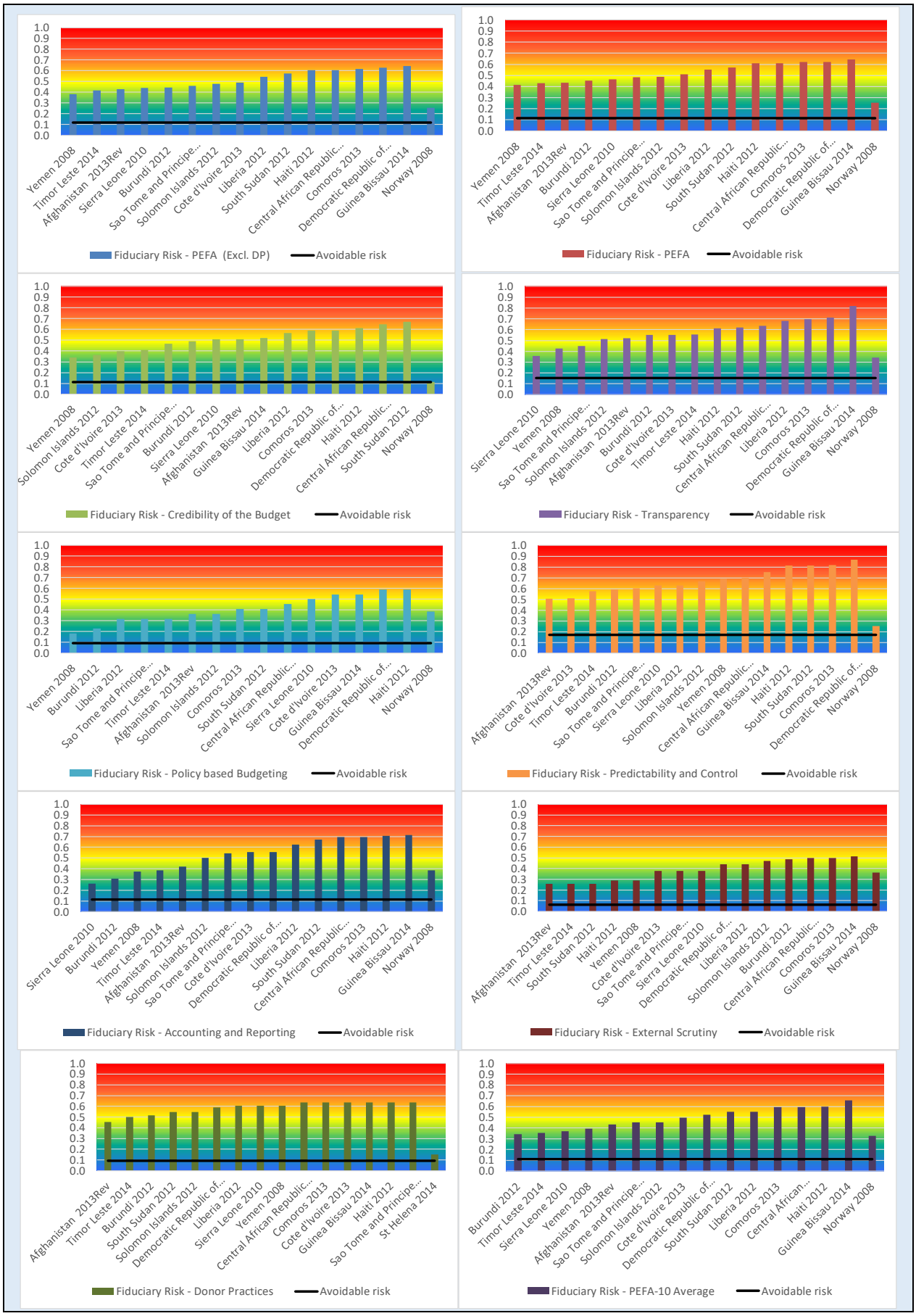


Figure 29. g7+ Fiduciary Risk Profiles

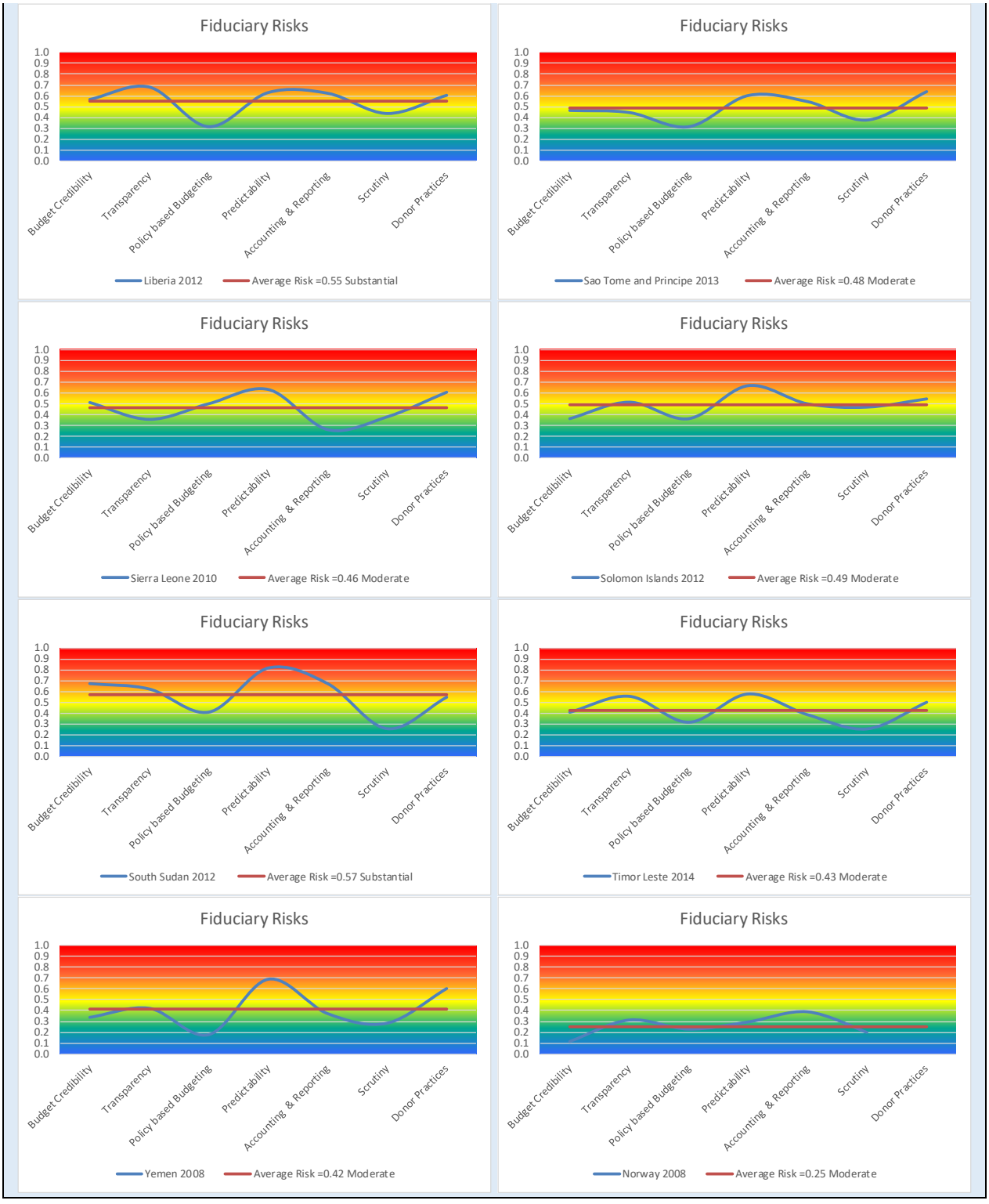
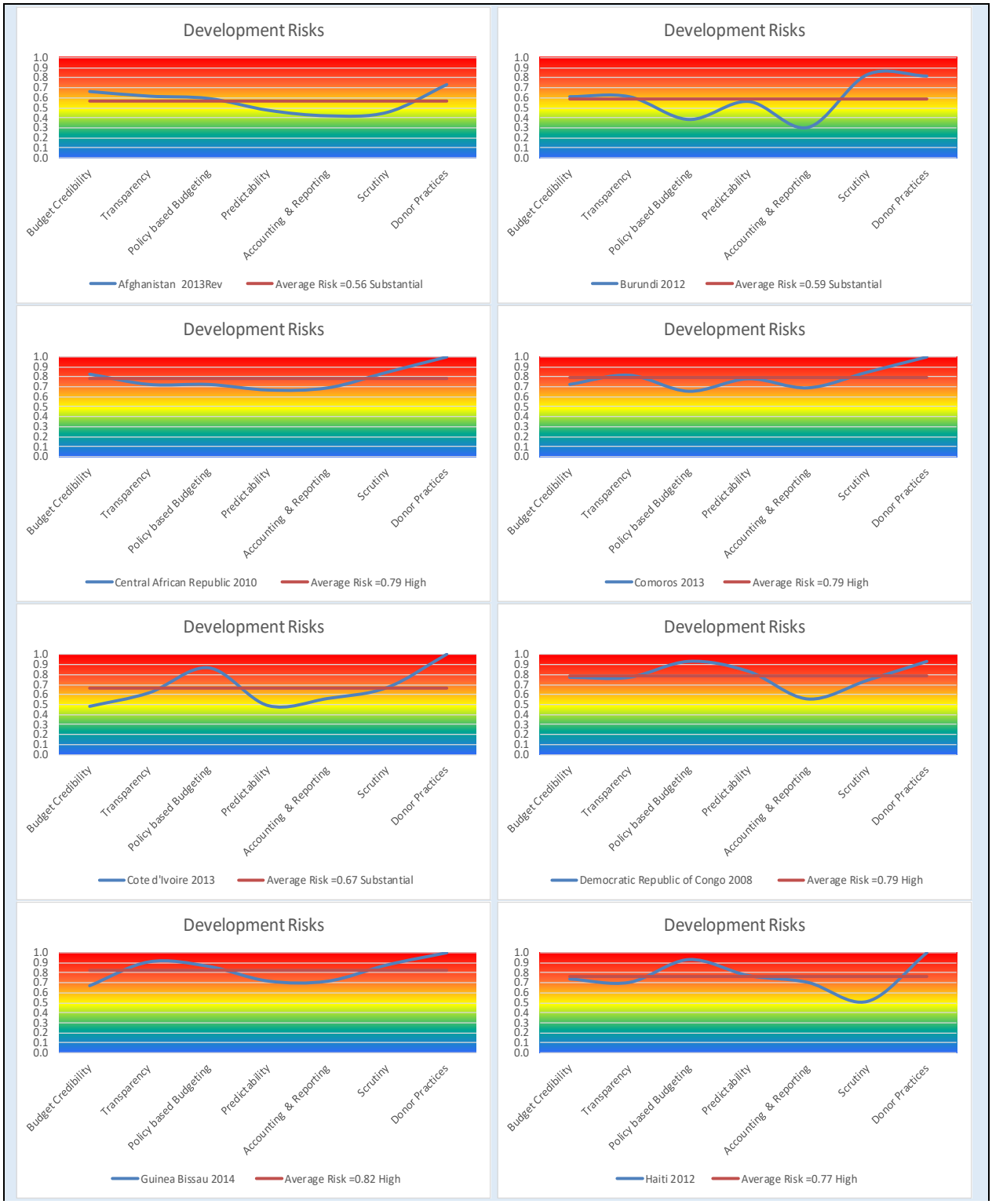
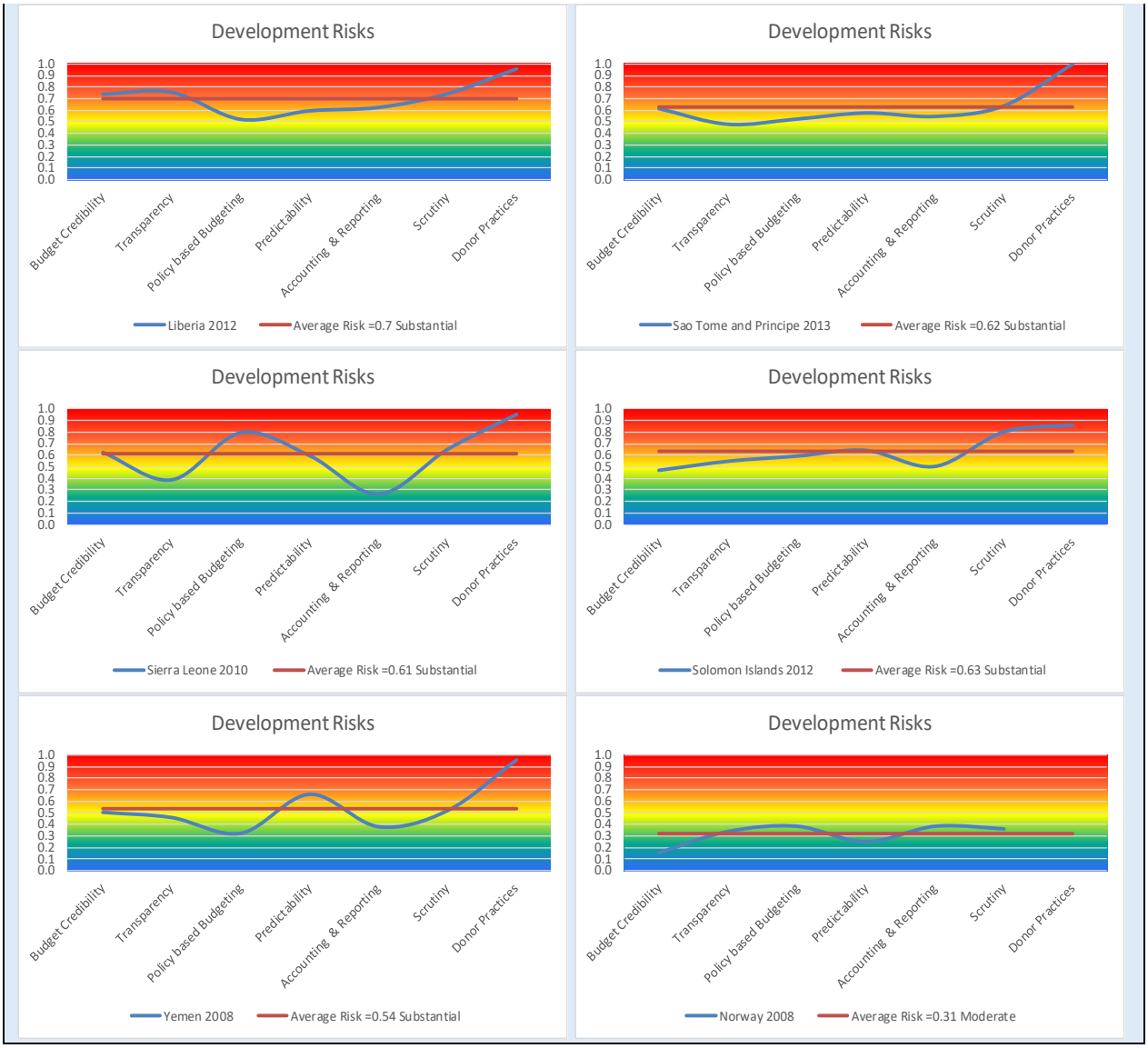

Fiduciary Risks
1.0 0.9 0.8 0.7 0.6 0.5 0.4 0.3 0.2 0.1 0.0
Budget Credibility
Transparency
Policy based Budgeting
Predictability
Accounting & Reporting
Scrutiny
Donor Practices
Liberia 2012
Average Risk =0.55 Substantial
Fiduciary Risks
Sao Tome and Principe 2013
Average Risk =0.48 Moderate
Fiduciary Risks
Sierra Leone 2010
Average Risk =0.46 Moderate
Fiduciary Risks
Solomon Islands 2012
Average Risk =0.49 Moderate
Fiduciary Risks
South Sudan 2012
Average Risk =0.57 Substantial
Fiduciary Risks
Timor Leste 2014
Average Risk =0.43 Moderate
Fiduciary Risks
Yemen 2008
Average Risk =0.42 Moderate
Fiduciary Risks
Norway 2008
Average Risk =0.25 Moderate

Figure 30. g7+ Country Development Risk Profiles




Development Risks
1.0
0.9
0.8
0.7
0.6
0.5
0.4
0.3
0.2
0.1
0.0
Budget Credibility
Transparency
Policy based Budgeting
Predictability
Accounting & Reporting
Scrutiny
Donor Practices
Liberia 2012
Average Risk =0.7 Substantial
Development Risks
Budget Credibility
Transparency
Policy based Budgeting
Predictability
Accounting & Reporting
Scrutiny
Donor Practices
Sao Tome and Principe 2013
Average Risk =0.62 Substantial
Development Risks
Budget Credibility
Transparency
Policy based Budgeting
Predictability
Accounting & Reporting
Scrutiny
Donor Practices
Sierra Leone 2010
Average Risk =0.61 Substantial
Development Risks
Budget Credibility
Transparency
Policy based Budgeting
Predictability
Accounting & Reporting
Scrutiny
Donor Practices
Solomon Islands 2012
Average Risk =0.63 Substantial
Development Risks
Budget Credibility
Transparency
Policy based Budgeting
Predictability
Accounting & Reporting
Scrutiny
Donor Practices
Yemen 2008
Average Risk =0.54 Substantial
Development Risks
Budget Credibility
Transparency
Policy based Budgeting
Predictability
Accounting & Reporting
Scrutiny
Donor Practices
Norway 2008
Average Risk =0.31 Moderate

End Reference

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