Public Disclosure Authorized

Public Disclosure Authorized

Document of
The World Bank

FOR OFFICIAL USE ONLY

Report No: PAD 1380

INTERNATIONAL DEVELOPMENT ASSOCIATION

PROJECT APPRAISAL DOCUMENT

ON A

SOMALIA MULTI-PARTNER FUND GRANT

IN THE AMOUNT OF US$24.0 MILLION EQUIVALENT

TO THE

FEDERAL REPUBLIC OF SOMALIA

FOR A

RECURRENT COST AND REFORM FINANCING PROJECT
PHASE II

June 23, 2015

Governance Global Practice
Africa Region

This document has a restricted distribution and may be used by recipients only in the performance of their official duties. Its contents may not otherwise be disclosed without World Bank authorization.

CURRENCY EQUIVALENTS

(Exchange Rate Effective June, 2015)

Currency Unit	=	Somali Shilling
Somali Shilling 844.5	=	US$1.00

FISCAL YEAR
January 1 – December 31

ABBREVIATIONS & ACRONYMS

AFDB	African Development Bank
AFS	Annual Financial Statements
AGE	Anti-Government Elements
AMISOM	African Union Mission to Somalia
ANRAP	Afghanistan National Rural Access Program
ANSP	Afghanistan National Solidarity Program
ARTF	Afghanistan Reconstruction Trust Fund
CBS	Central Bank of Somalia
CCSD	Global Center for Conflict, Security and Development
CIM	Capacity Injection Mechanism
CIP	Capacity Injection Project
CIT	Component Implementation Team
CPFMRP	Cambodia Public Financial Management Reform Project
CQS	Consultant Qualification Selection
CSC	Civil Service Commission
CTRLA	Controllers Department, World Bank
DA	Designated Account
DCTT	Directorate of Customs, Taxation & Treasury
DEO	District Education Officer
DRC	Directorate of Revenue Collection
EAFS	External Assistance Fiduciary Section (in Office of Accountant General)
ERP	Economic Recovery Plan
EMIS	Education Management Information System
EPBS	Ethiopia Protection of Basic Services Project
ESSP	Education Sector Strategic Plan
FBS	Fixed Budget Selection
FCS	Fragile and Conflict Affected Situation
FGC	Financial Governance Committee
FGS	Federal Government of Somalia
FMU	Financial Management Unit (under the Norway SFF)
FRS	Federal Republic of Somalia
GER	Gross Enrollment Ratio
GPE	Global Program for Education
GPI	Gender Parity Index
HIPC	Heavily Indebted Poor Country Initiative
HRM	Human Resource Management

IC	Individual Consultant
IE	Impact Evaluation
IDP	Internally Displaced Person
IFR	Interim unaudited Financial Report
IJA	Interim Jubba Administration
IPSAS	International Public Sector Accounting Standards
ISA	International Standards on Auditing
ISN	Interim Strategy Note
JHNP	Joint Health and Nutrition Program
LCS	Least Cost Selection
MDA	Ministries, Departments and Agencies
MDGs	Millennium Development Goals
M&E	Monitoring and Evaluation
MoF	Ministry of Finance
MPF	Multi Partner Fund
NCSC	National Civil Service Commission
NDEFS	New Deal for Engagement in Fragile States
OAG	Office of the Accountant General
OAuG	Office of the Auditor General
OB	Oversight Board
ODA	Overseas Development Assistance
OT	Operating Team
PDO	Project Development Objective
PEFA	Public Expenditure Financial Assessment
PFM	Public Financial Management
PFMCSP	Public Financial Management Capacity Strengthening Project
PFMRCU	Public Financial Management Reform Coordinating Unit
PL	Puntland Member State of Somalia Federal Republic
PSG	Peace and State-Building Goals
PTR	Pupil Teacher Ratio
PWC	Price Waterhouse Coopers
QBS	Quality Based Selection
QCBS	Quantity and Cost Based Selection
RCRFP	Recurrent Cost and Reform Financing Program
REO	Regional Education Officer
RETF	Recipient-Executed Trust Fund
RDP	Reconstruction and Development Program for Somalia
SCoA	Standard Chart of Accounts
SDRF	Somalia Development and Reconstruction Facility
SFF	Special Financing Facility (Norway)
SFMIS	Somalia Financial Management Information System
SLPAPP	Sierra Leone Pay and Performance Project
SME	Subject Matter Expert
SMP	Staff-Monitored Program
SOP	Series of Projects
SORT	Systematic Operations Risk-rating Tool
SPF	State and Peace-Building Fund
SPSDRP	Somalia Private Sector Development Reengagement Project
SSF	Somalia Stability Fund

SSL	Secure Sockets Layer
SSS	Single Source Selection
StAR	Stolen Asset Recovery Initiative
TAS	Treasury Accounting System
TFG	Transitional Federal Government
TICPI	Transparency International Corruption Perception Index
TSA	Treasury Single Account
TSC	Technical Steering Committee
UCS	Use of Country Systems
UNDP	United Nations Development Program
UNFPA	United Nations Family Planning Association
UNHCR	United Nations High Commissioner for Refugees
UMMPTF	United Nations Multi-Partner Trust Fund
WBG	World Bank Group
WDR	World Development Report

Regional Vice President:	Makhtar Diop
Country Director:	Bella Bird
Senior Global Practice Director:	Mario Marcel Cullell
Practice Manager:	Renaud Seligmann
Task Team Leader:	Adenike Sherifat Oyeyiola
Co-Task Team Leader	John Randa

PAD DATA SHEET

Somalia

Recurrent Cost & Reform Financing Project: Phase II (154875)

PROJECT APPRAISAL DOCUMENT

AFRICA

Report No.: PAD 1380

Basic Information			
Project ID	EA Category	Team Leader	
P154875	C - Not Required	Adenike Sherifat Oyeyiola	
Lending Instrument	Fragile and/or Capacity Constraints [X]		
Investment Project Financing	- Fragile States	- Post-Conflict	
	Financial Intermediaries [ ]		
	Series of Projects [X]		
Project Implementation Start Date	Project Implementation End Date		
25-June-2015	30-June-2020		
Expected Effectiveness Date	Expected Closing Date		
29-June-2015	30-June-2020		
Joint IFC			
No			
Practice Manager	Senior Global Practice Director	Country Director	Regional Vice President
Renaud Seligmann	Mario Marcel Cullell	Bella Bird	Makhtar Diop

Approval Authority
Approval Authority
RVP Decision

Borrower: Ministry of Finance			
Responsible Agency : Ministry of Finance			
Contact:	H.E. Mohamed Aden Ibrahim	Title:	Minister of Finance

Telephone No:	252612777738	Email: farkeeti@hotmail.com

Project Financing Data(in US$ Million)

[ ]	Loan	[ ]	IDA Grant	[ ]	Guarantee
[ ]	Credit	[X]	Grant	[ ]	Other

Total Project Cost:	**144.0**	Total Bank Financing:	144.00
Financing Gap:	0.0		

Financing Source	Amount
Borrower	**0.0**
Somalia Multi-Partner Fund (MPF)	144.0
Other financing	0.0
Total	**144.0**

Expected Disbursements (in $ Million)

Fiscal Year	2015	2016	2017	2018	2019	2020				
Annual	24	30	30	30	**25**	5				
Cumulative	24	54	84	114	**139**	144				

Development Objective(s)

The Development Objective for the Series of Projects (SOP) is to enable the Somali Government to achieve reliable and transparent financing of critical civil service operations to help strengthen the legitimacy of the state.

The Development Objective of this second project is to support the government to provide credible and sustainable payroll and to establish the foundation for efficient budget execution and payment systems for the non-security sectors in Federal Government of Somalia (FGS) and eligible federal member states, interim and emerging administrations.

This aligns with the MPF objective “to foster socio-economic recovery and stabilization by supporting the payment of civil service salaries, and the running costs of government institutions; financing technical assistance and supporting the building blocks of larger public investment programs across a range of sectors.”

Components	
Component Name	**Cost ($ Millions)**
Support to core government functions of ministries, department & agencies (MDAs) of Federal Government of Somalia	81.0
Inter-governmental fiscal transfers for core functions in eligible federal member states, interim and emerging administrations	34.0
Support to recurrent costs in education and health sectors in FGS and eligible federal member states, interim and emerging administrations	20.0
Project management and coordination	9.0
Total	**144.0**

Institutional Data

Practice Area / Cross Cutting Solution Area

Governance

Cross Cutting Areas

[ ]	Climate Change
[X]	Fragile, Conflict & Violence
[ ]	Gender
[ ]	Jobs
[ ]	Public Private Partnership

Sectors / Climate Change

Major Sector	Sector	percentage	Adaptation Co-benefits percentage	Mitigation Co-benefits percentage
Public Administration, Law, and Justice	Central government administration	25		
Public Administration, Law, and Justice	Sub-national government administration	15		
Public Administration, Law, and Justice	Public administration-Education	10		
Public Administration, Law, and Justice	Public administration-Health	10		
Public Administration, Law, and Justice	General public administration sector	40		
Total		100		

☑ I certify that there is no Adaptation and Mitigation Climate Change Co-benefits information applicable to this project.

Themes

Major theme	Theme	Percentage
Public sector governance	Administrative and civil service reform	60
Public sector governance	Other public sector governance	20
Public sector governance	Public Financial Management	10
Social Development, Gender and Inclusion		10
Total		100

Systematic Operations Risk- Rating Tool (SORT)

Risk Category	**Rating**
1. Political and governance	Substantial
2. Macroeconomic	High
3. Sector strategies and policies	Substantial
4. Technical design of project or program	Substantial
5. Institutional capacity for implementation and sustainability	Substantial
6. Fiduciary	High
7. Environment and social	Low
8. Stakeholders	Substantial
9. Other	High
OVERALL	**High**

Compliance

Policy

Does the project depart from the CAS in content or in other significant respects?	Yes [ ]	No [X]
Does the project require any waivers of Bank policies?	Yes [ ]	No [X]
Have these been approved by Bank management?	Yes [ ]	No [ ]
Is approval for any policy waiver sought from the Board?	Yes [ ]	No [X]
Does the project meet the Regional criteria for readiness for implementation?	Yes [X]	No [ ]

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01		X
Natural Habitats OP/BP 4.04		X
Forests OP/BP 4.36		X
Pest Management OP 4.09		X
Physical Cultural Resources OP/BP 4.11		X
Indigenous Peoples OP/BP 4.10		X
Involuntary Resettlement OP/BP 4.12		X
Safety of Dams OP/BP 4.37		X
Projects on International Waterways OP/BP 7.50		X
Projects in Disputed Areas OP/BP 7.60		X

.

Conditions

Source of Fund	Name	Type
AFS2	Somalia Multi Partner Fund (MPF)	Disbursement

Description of Condition

In accordance with Section 3.02 of the Standard Conditions, the World Bank's payment obligations in connection to the MPF Agreement are limited to the amount of funds made available to it by the donors under the above mentioned trust fund, and the Recipient's right to withdraw the Grant proceeds is subject to the availability of such funds.

Effectiveness Conditions

Source of Fund	Name	Type
AFS2	Project Steering Committee and Project Management Team	Effectiveness

Description of Covenant:
The Recipient has established the Project Steering Committee and the Project Management Team in accordance with the provisions of Section I.A of Schedule 2 to the Grant Agreement.

Source of Fund	Name	Type
AFS2	Project Operation Manual	Effectiveness

Description of Covenant:
The Recipient has prepared and adopted a Project Operations Manual in accordance with the provisions of Section I.B.1 of Schedule 2 to the Grant Agreement.

Team Composition

Bank Staff

Name	**Title**	**Specialization**	**Unit**
Adenike Sherifat Oyeyiola	Senior Financial Management Specialist	Team Leader	GGODR
John Randa	Senior Economist	Co- Team Leader	GMFDR
Huihui Wang	Senior Economist	Health Sector	GHNDR
Nalin Jena	Senior Education Specialist	Education Sector	GEDDR
Thilasoni Benjamin Musuku	Senior Financial Sector Specialist	Financial Sector	GFMDR
Geoff Handley	E T Consultant	Macro & Fiscal	GGODR
Stephen Mugendi Mukaindo	Counsel	Legal	LEGAM
Christiaan Johannes Nieuwoudt	Finance Officer	Disbursement	CTRLA
Donald Mphande	Lead Financial Management Specialist	Financial Management in Conflict & Fragile States	GCFDR
Diego Garrido Martin	Senior Operations Officer	Monitoring and Evaluation	GCFDR
Wolfhart Pohl	Adviser	Safeguards	GCFDR
Marie J. Bolou	Senior Operations Assistant	Program Support	GGODR
Agnes Yvonne Masaka	E T Temporary	Team Administration	GGODR
Winston Cole	Senior Financial Management Specialist	Public Financial Management	GGODR
Stephan Massing	E T Consultant	Civil Service	GGODR
Yoko Kagawa	Senior Operations Officer	Monitoring and Evaluation	GPSOS
Non-Bank Staff			
Leonard Mutuku Matheka	Consultant	Financial Management	GGODR
John Etidau	Consultant	Procurement	GGODR
Leonard Mawiooj	Consultant	Risk management	GGODR
Richard A. Cambridge	Consultant	Operations Adviser	GGODR
Ousman Abdulahi Ali	Consultant	Macro-Economics	GFMDR
Salome Aganda	E.T Temporary	Program Support	AFCE4
Locations			

Country	First Administrative Division	Location	Planned	Actual	Comments
Federal Republic of Somalia	Mogadishu	Mogadishu			Security Concerns
Federal Republic of Somalia	Puntland	Puntland			Security Concerns
Federal Republic of Somalia	Interim Jubba Administration	Jubbaland			Security Concerns

FEDERAL REPUBLIC OF SOMALIA

Recurrent Cost and Reform Financing Project: Phase 1I

Table of Contents

ANNEXES

TABLES

FIGURES

I. STRATEGIC CONTEXT

A. Country Context

1. **Somalia has been in conflict for over twenty years**. Since the collapse of the Siad Barre government in 1991, southern Somalia has experienced cycles of conflict that fragmented the country, destroyed legitimate institutions and created widespread vulnerability. Between 1988 and 1993, civil war destroyed Mogadishu and Hargeisa, resulted in massive civilian deaths and exacerbated the 1991 famine that had thousands of victims. Peace conferences finally led to the formation in 2000 of the Transitional National Government, and then the Transitional Federal Government in 2004, though a still unconducive environment for constructive and productive development. In 2012, there was a peaceful and legal transfer of power from the transitional to a full-fledged federal government in Mogadishu, with a four-year term under a provisional constitution approved by an appointed parliament. This generated domestic political momentum and triggered international re-engagement. Regional countries and international actors have strengthened their efforts to support and sustain this window of opportunity, endorsing a New Deal[1] for Somalia at the September, 2013 Brussels Conference and pledging US$2.4 billion against a set of five priority Peace-building and State-building Goals (PSG) set out in a Somali Compact (Compact)[2] and the Somaliland Special Arrangement. The Compact preparation process sought to be inclusive of Somalia's different regions and communities and also establish a new aid framework- the Somalia Development and Reconstruction Facility (SDRF), which provides a single governance platform for coordinating international assistance with Compact priorities delivered through windows administered by technical agencies (including the World Bank).

2. **In contrast to the war-torn south, northern areas have put in place functioning institutions that have succeeded in sustaining stability, although considerable development challenges remain**. Somaliland and Puntland have developed hybrid forms of governance, which have guaranteed higher levels of peace, security and institutional development. While substantial development challenges remain, the starting point for development work is nevertheless different in the north.

3. **Somalia has experienced a rapid, fluid and complex process of political agreements for emerging federal member states**. The Federal Government of Somalia (FGS) is leading political dialogue with regional entities as a basis for incremental state formation within a federal model. Starting with the August 27, 2013 Addis Ababa agreement on the formation of the Interim Juba Administration (IJA), this process has led the FGS to articulate a framework within which Somalia's resources, including international assistance, are shared between the levels of government- in line with agreements on administrative and functional assignments. As a result of the de facto highly devolved revenue and expenditure assignments that have developed in Somalia, the delivery of basic public services currently takes place at a sub-national level. Similarly, the Puntland constitution of 2009 amended and approved by parliament on April 18, 2012 specifies that Puntland is committed to participate in Somalia's federal system. Pending the completion of the federal constitution ratified by Puntland and approved by a popular referendum, Puntland state shall have the status of an independent state. It was agreed that Puntland's priorities for revenue and public financial management reforms (2014-2016) should be taken into account in the Somali Compact and

[1] http://www.somalia-newdeal-conference.eu/
[2] The five PSGs are inclusive politics, security, justice, economic foundations and revenue & services.

that Puntland's participation in the New Deal aid architecture was important- particularly in the Somali Development and Reconstruction Facility (SRDF).

4. The Interim Jubba Administration (IJA); Interim Southwest Administration and the Banadir Region have been formed. Two more emerging states are being formed.

5. **With years of conflict and low investments in health, Somalia is ranked comparatively low globally on various health indicators and is off-track to achieve health-related Millennium Development Goals (MDGs).** Globally, it ranks second highest for total fertility rate (6.3), fourteenth lowest for life expectancy at birth (51), and second highest for maternal mortality ratio (1,000 per 100,000 live births). Coverage of essential health services is very low in Somalia.

6. **Somalia continues to face complex and multidimensional challenges in the areas of curriculum, teacher training, school infrastructure, lack of public education, unregulated private education, school finance and untrained educational professionals**. A recent Heritage Institute Report[3] highlights the fact that the most pressing challenges facing the education system include: addressing the current curriculum chaos by developing a national curriculum; resolving such teacher-related challenges as improvement in pedagogical and teaching skills; designing a teacher pay structure and addressing the broad teacher shortage.

7. **Despite the increase in the number of schools, enrollment and the pupil-teacher ratio since 2006 in both Somaliland and Puntland is far below the Sub-Saharan Africa average.** In Somaliland, the gross enrollment ratio (GER) at the primary level is 44 percent, with the GER for boys and girls at 50 percent and 38 percent respectively. Although the teachers' cohort has continued to grow, the pupil teacher ratio (PTR) stands at 31:1, with significant regional disparities. The Gender Parity Index (GPI) increased from 2006, with the GPI as high as 0.8; and gender gaps continue at all levels in education sectors. The status of primary education in Puntland is quite similar to Somaliland. There's no data available on either completion rates or learners' achievements.

8. **While transition rates from grade 8 have increased, the increase in the number of pupils in primary schools, combined with limited investment in expanding the secondary education provision, has resulted in a serious bottleneck**. Over 55 percent of children in the 6-13 age-group are out of school and about 21 percent of youth (age 14-29) are neither working nor in schools. Though Somalia is a young country, with over 70 percent of the population under the age of 30 and a growing youth population, there are inadequate education and skills-development programs to provide a second chance for out-of-school youth. This poses a huge challenge to the socio-economic development of Somalia. These challenges are further accentuated by gender disparities, especially in lower secondary schools with only 28 percent of girls transitioning to such schools.

9. **In Puntland State, the government has made some significant progress in the education sector in the last few years.** A revised Education Sector Strategic Plan (ESSP) for the period 2014-16 covering the whole spectrum from early childhood education to tertiary/higher education has been developed. The key focus of the Strategic Plan is to improve the outcomes of the education sector by enhancing investment and strengthening governance, policy and the institutional framework of the education system[4]. The objectives of

[3] http://www.heritageinstitute.org/wp-content/uploads/2015/04/Educational-challenges-in-post-transitional-Somalia_ENG.pdf

[4] The key challenges that the ESSP identifies include: (i) a decentralized system with low capacity, (ii) inequality of access to education; (iii) low capacity for efficient teacher management; (iv) inadequate financing; and (v) low capacity for policy development. In the context of these challenges, financing of salaries of teachers, head teachers, District Education Officers

the ESSP are clearly aligned with the overall objectives of the proposed Recurrent Cost and Reform Financing Project: Phase II (RCRF II).

B. Economic and Sectoral Context

10. **Somalia's economy has been shaped by sustained conflict and remains vulnerable to shocks.** In the absence of state regulation and institutions, a vibrant informal sector has developed, boosted by approximately US$1.3 billion in annual remittances from the roughly one million Somalis living in the Diaspora.[5] While the informal sector has thrived, the absence of regulation coupled with elite capture in key economic sectors undermines the inclusiveness of economic development. Somalia is highly reliant on Overseas Development Assistance (ODA). Development partners finance more than half of the government budget. Budget support for 2014 totaled US$87.0 million (51 percent), compared with US$82.0 million in domestic revenue (data as of October, 2014). Total aid to Somalia has hovered around US$1.0 billion since 2011; however, an increasing proportion of this aid is being directed toward longer-term development in Somalia under the New Deal, as evidenced by donor reporting of 2014-15 planned disbursements to the Aid Coordination Unit of the FGS.[6]

11. **Somalia's overall macroeconomic situation is very difficult to assess because of severe data limitations**. Accurate national accounts data do not yet exist for the whole of Somalia. However, Gross Domestic Product (GDP) in 2014 was estimated at approximately US$5.7 billion, comprising US$1.8 billion for Somaliland and US$3.9 billion for southern Somalia, including Puntland. Public expenditure is estimated to account for 6.5 percent of GDP, compared with private sector consumption of 138 percent of GDP; agriculture and services are the key contributors to GDP. Somalia's trade deficit is estimated to have grown in recent years, reaching more than US$2.5 billion in 2014, up from US$165.0 million in 2000 (financed by assistance and remittances). Imports consist mainly of manufactured and petroleum products from regional trading partners. The exchange rate is volatile and has appreciated against the dollar in 2013 with inflows of investment and aid- leading to a Dutch disease problem. The shillings in circulation are old, depreciated, and, in some instances, counterfeit, which limits their use in transactions. The economy is largely dollarized and the Somali shilling is used only for smaller transactions. With little or no control over the domestic money supply, and little foreign reserves, the Central Bank has no influence over the exchange rate.

12. **Revenue growth was very robust in 2013 and 2014. Revenue and grants outturns in 2014 increased by 29 percent (US$33.9 million), in nominal terms over 2013 figures.** The increase was as a result of tax revenues, which increased by 23 percent (US$14.8 million), and non-tax revenue that increased by 302 percent (US$12.6 million). Taxes on incomes, goods and services, and trade increased by 54, 51 and 20 percent, respectively, in 2014. As a share of GDP, revenues and grants increased from 1.0 percent in 2012 to 3.8 percent in 2014-almost four times the 2012 level.

13. **The FGS revenue forecasts in the 2015 budget were unrealistically high when compared to both the 2013 and 2014 outturns.** The 2014 budget revenue projection was US$188.0 million, a 60 percent increase from the 2013 outturn of US$117.0 million. The

---

and Regional Education Officers and non-salary recurrent costs would be targeted toward supporting the Government of Puntland in addressing these challenges, in general and strengthening the education system in a sustainable manner, in particular

[5] Orozco, Manuel and Julia Yansura (2013), "Keeping the Lifeline Open: Remittances and Markets in Somalia," Oxfam.

[6] ACU/WB (2014), "Aid Flows in Somalia: Analysis of aid flow data," Federal Government of Somalia.

revenue outturn for 2014 was US$151.0 million, a shortfall of US$37.2 million or 20 percent on budgeted levels. The 2014 budget was predicated on significant increases in revenue from income and corporate taxes, and taxes on goods and services, but this did not fully materialize.

Table 1: FGS Revenue Performance 2012-2015

	2012	2013		2014		2015	Growth in Revenue	
(Million US$)	Actual	Budget	Actual	Budget	Preliminary	Budget	2012-2013	2013-2014
Revenue and Grants	**35.1**	**114.3**	**117.4**	**188.5**	**151.3**	**239.9**	**234%**	**29%**
Domestic Revenue	**30.2**	**53.9**	**75.8**	**115.3**	**96.3**	**123.4**	**151%**	**27%**
Tax Revenue	**25.3**	**51.4**	**65.1**	**108.0**	**79.8**	**103.1**	**157%**	**23%**
Tax on Income, Profit and Capital Gains		3.5	0.7	5.1	1.1	4.6		**57%**
Taxes on goods and services	1.3	14.4	5.6	33.9	8.5	25.8	**331%**	**52%**
Trade taxes	24.0	33.4	58.7	69.0	70.3	72.7	**145%**	**20%**
Non-Tax Revenue		2.5	4.1	7.3	16.5	20.3		**302%**
Domestic loan and grants	0.0	0.0	6.6	0.0	0.0			**-100%**
Grants	**4.9**		**41.7**	**73.2**	**55.0**	**116.5**	**751%**	**32%**
Bilateral	4.9		41.7	64.0	53.1	39.9	**751%**	**27%**
Multilateral			0.0	9.2	1.8	76.7		
	% of GDP							
Revenue and Grants	**1.0**	**3.1**	**3.2**	**4.8**	**3.8**	**5.9**		
Domestic Revenue	**0.9**	**1.5**	**2.1**	**2.9**	**2.4**	**3.0**		
Tax Revenue	**0.7**	**1.4**	**1.8**	**2.7**	**2.0**	**2.5**		
Tax on Income, Profit and Capital Gains	-	0.1	0.0	0.1	0.0	0.1		
Taxes on goods and services	0.0	0.4	0.2	0.9	0.2	0.6		
Trade taxes	0.7	0.9	1.6	1.8	1.8	1.8		
Non-Tax Revenue	-	0.1	0.1	0.2	0.4	0.5		
Domestic loan and grants	-	-	0.2	-	-	-		
Grants	**0.1**	**-**	**1.1**	**1.9**	**1.4**	**2.9**		
Bilateral	0.1	-	1.1	1.6	1.3	1.0		
Multilateral	-	-	-	0.2	0.0	1.9		
Memorandum:								
Total GDP (Current US$ Millions)	**5,008**	**5,352**	**5,352**	**5,706**	**5,706**	**5,953**		
Somaliland	1,550	1,657	1,657	1,771	1,771	1,894		
Somalia (excluding Somaliland)	3,458	3,695	3,695	3,935	3,935	4,059		

Source: Ministry of Finance, FGS - (Appropriation Act for 2015 Budget and various budget documents)

14. **Domestic revenue (excluding grants) increased by 27 percent in 2014.** Revenue from domestic sources increased from US$75.8 million in 2013 to US$96.3 million in 2014. This enhanced revenue enabled the financing of 64 percent of recurrent expenditures. Taxes on income underperformed by 78 percent while those from goods and services underperformed by 75 percent with combined revenue from these sources realising US$9.6 million against a target of US$39.0 million. Grants generated US$55.0 million against a target of US$73.2 million.

15. **Forecasting revenues in Somalia is an onerous task due to data challenges.** Mobilization of revenues is a function of a number of macro indicators, the knowledge of which enables reasonable estimates and trend-of-revenue performance. The challenge for Somalia is that, over time, reliable estimates do not exist for most of these macro-indicators- despite the fact that reliable fiscal data disaggregated by sources only started being released in 2013. As such, there are no time series that can enable robust revenue projections.

16. **Despite data limitations, it seems clear that the 2015 revenue estimates projected at US$240.0 million (i.e. 59 percent above 2014 preliminary collections) are unrealistically high**. The FGS has drawn out revenue measures it will undertake in 2015 to support increased collections. Revenue mobilization is expected to soar in 2015 from income and corporate taxes, and sales and telecommunications taxes. An analysis of the government plan indicates that while there is scope for an increase of these revenues if there is political will to improve

collection, it is unlikely that the totality of the expected increase will materialize in 2015. This optimistic revenue estimate conceals a continued structural fiscal shortfall driven by the desire to hire more civil servants without regard for budget constraints**.** Revenue forecasts in 2015 are estimated to increase 29 percent, the same rate as in 2014.[7] Revenue is projected to increase to US$195.0 million in 2015.[8] From a budget implementation perspective, there will therefore be a significant shortfall (US$45.0 million) that will require cutbacks to expenditures approved by parliament through 'cash rationing' during budget execution.

17. **A realistic revenue estimate of US$195.0 million will be adequate to meet all categories of expenditure except costs of arrears repayment.** Assuming the same 85 percent budget execution rate for compensation of employees during 2015, as was the case in 2014, monthly cash expenditures on employees could be around US$7.7 million, or about 47.5 percent of monthly revenue under a realistic scenario. Approximately US$102.0 million would then remain (after paying wages, salaries and allowances) to finance other lines of the budget. Revenues would cater for Goods and Services (budgeted at US$80.5 million), Grants (budgeted at US$16.0 million) and Contingencies. However, budget funds would not be enough to cover repayment of arrears on the order of US$17.0 million, as well as capital spending of US$13.9 million, since only US$2.3 million would be available. Hence, the RCRF II operation in 2015 at the FGS level is both supportive of the predictable payment of civil service salaries while also creating fiscal space for non-salary operating expenditures to enable government to provide basic services to the citizens.

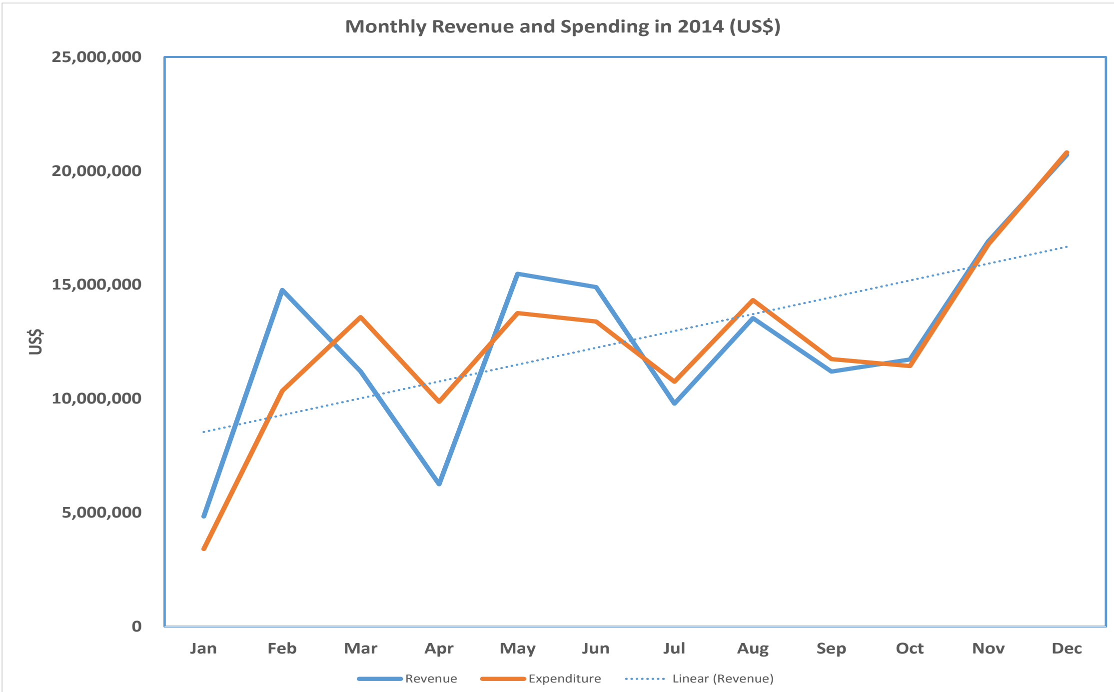
18. **The extent of further accumulation of arrears during 2015 will depend in large part on how quickly commitment controls can be introduced into the payment process and the Somalia Financial Management Information System (SFMIS) during 2015**. The strengthening of the non-salary payment process controls is therefore of material fiscal importance. Since revenues are likely to fall short of the legally appropriated expenditure levels, the 2015 budget needs to be revised. The government also needs commitment control system to avoid further arrears accumulation. Commitment control is however a major aspect of the SFMIS.

19. **The FGS needs to strengthen its revenue mobilization efforts with a strong focus on planning and the required human and financial resources that could result in significant revenue increases.** The Public Financial Management (PFM) strengthening project is supporting government in revenue administration that focuses on improving tax mobilization; including, sequencing and a timetable and likely resourcing implications for reform actions sufficient to provide an adequate revenue base for FGS. In addition, this project is providing the needed capacity enhancements through the payment of salaries of civil servants needed to support the government's revenue generation activities.

[7] In the base scenario, the same institutions (who are now in the tax bracket) which paid taxes last year continues to do so in 2015. It also assumes that the economic growth in 2015 is the same rate as in 2014.

[8] Budget execution in 2015 was at 80%. If this rate is maintained in 2015, this will yield revenues at US$192 million

Figure 1: **FGS Revenue Trends in 2014**



Source: FGS Ministry of Finance

20. **Monthly expenditures have closely matched monthly revenues during 2014, reflecting the cash-based nature of budget management**. Expenditures have averaged US$12.5 million per month, while revenues have averaged US$12.6 million per month. Budget figures in 2014 suggest that total monthly expenditures on compensation of employees (including security sector allowances), amount to an average of US$6.4 million per month. This mainly comprises wages and salaries at US$2.0 million, and allowances at US$4.3 million. In September 2014, the RCRF Phase I project reimbursed US$1.4 million in compensation to employees (both wages/salaries and allowances of eligible civil servants), equivalent to 57.5 percent of the budget level and 71.7 percent of actual monthly spending on wages and salaries. Figure 1 indicates that at the beginning of the year, revenues and expenditures outturns tend to be slow but this picks up towards the end of the year.

21. **FGS expenditures are dominated by wages and salaries, which accounted for 44 percent and 51 percent of expenditures in 2013 and 2014 respectively.** The next largest category of expenditure is goods and services, which accounted for 46 percent and 38 percent of 2013 and 2014 expenditures. However, operating expenditures are primarily concentrated in the security sector and most line ministries have very little funding available for operating expenditures; for example, only 5 percent of education and 14 percent of health spending was dedicated to operating costs in 2014**.**

22. **The major spending organisation during 2014 was the Armed Forces, with 28.8 percent of actual spending, or US$43.3 million,** and with over half accounted for by allowances (US$20.9 million). There has been a progressive build-up of arrears in general but more in the armed forces- which signals a lack of expenditure control and undermine the credibility of the budget. Arrears at the end of 2013 were US$30.4 million (16.1 percent of the

budget), which were carried into the 2014 budget. However, only US$1.3 million was paid in 2014 and an additional US$13.8 million accrued, mostly for wages and salaries of FGS employees. The build-up of arrears is not a good signal and affects service-delivery. As of the end of 2014, the estimated stock of outstanding arrears was US$43.0 million.

Table 2: Total Disaggregated Government Expenditure for the 2012-2014 Period.

(Million US$)	2012 Actual	2013 Budget	2013 Actual	2014 Budget	2014 Preliminary	2015 Budget	Growth in Expenditure 2012-2013	Growth in Expenditure 2013-2014
Total Expenditure	**35.1**	**143.9**	**117.4**	**216.2**	**151.1**	**239.9**	**235%**	**29%**
Recurrent Expenditure	**35.1**	**136.7**	**117.4**	**203.9**	**137.1**	**226.0**	**235%**	**17%**
Compensation of employees	13.5	70.4	51.9	91.0	77.2	109.4	285%	49%
Use of goods and services	18.9	62.7	54.5	67.4	57.6	80.5	189%	6%
Grants	2.7	0.0	7.5	11.5	10.1	16.0	177%	35%
Contingency	0.0	3.6	3.5	3.6	37.8	3.2	n/a	973%
Repayment of arrears and advances	0.0	0.0	0.0	30.4	2.2	17.0	n/a	n/a
Capital Expenditure	**0.0**	**7.2**	**0.0**	**12.4**	**0.2**	**13.9**	n/a	n/a
Capital	0.0	7.2	0.0	12.4	0.2	13.9	n/a	n/a
% of GDP (excluding Somaliland)								
Total Expenditure	**1.0**	**3.9**	**3.2**	**5.5**	**3.8**	**5.9**		
Recurrent Expenditure	**1.0**	**3.7**	**3.2**	**5.2**	**3.5**	**5.6**		
Compensation of employees	0.4	1.9	1.4	2.3	2.0	2.7		
Use of goods and services	0.5	1.7	1.5	1.7	1.5	2.0		
Grants	0.1	0.0	0.2	0.3	0.3	0.4		
Contingency	0.0	0.1	0.1	0.1	1.0	0.1		
Repayment of arrears and advances	0.0	0.0	0.0	0.8	0.1	0.4		
Capital Expenditure	**0.0**	**0.2**	**0.0**	**0.3**	**0.0**	**0.3**		
Capital	0.0	0.2	0.0	0.3	0.0	0.3		
Memorandum:								
Total GDP (Current US$ millions)	**5,008**	**5,352**	**5,352**	**5,706**	**5,706**	**5,953**		
Somaliland	1,550	1,657	1,657	1,771	1,771	1,894		
Somalia (excluding Somaliland)	3,458	3,695	3,695	3,935	3,935	4,059		

Source: FGS Ministry of Finance

23. **In line with revenue projections, expenditure is projected at US$240.0 million in the 2015 budget, an increase of US$88.9 million on the 2014 estimated outturn (60 percent)**. The main components of the increase in expenditure are: (i) a 42 percent (US$32.0 million) increase in compensation of employees; (ii) a 40 percent (US$22.9 million) increase in goods and services; (iii) a 1,280 percent (US$15.7 million) increase in repayment of arrears and advances. These increases are unlikely to be fully realized during budget execution due to anticipated revenue shortfalls.

24. The increase in compensation of employees is particularly important to note because of its non-discretionary nature. The increase is driven by: (i) a US$2.0 million increase in wages and salaries, including a planned 20 percent increase in the number of civil servants from 3,756 to 4,486- which poses a fiscal risk and would contribute to arrears build-up; and, (ii) a US$10.0 million increase in allowances concentrated on 15 organizations, with security sector organizations receiving the biggest increases.

25. **In addition to the public workforce captured in budget documentation, development partners currently pay health and education workforces off budget.** They have significantly greater geographic dispersion than those currently on budget. In the case of

education, the Global Partnership for Education (GPE) pays US$100.0 matched by the government to 1,400 teachers through a government payroll process managed by the Ministry of Education. In the case of health, workers are paid through implementing partner agencies.

26. **However, the Ministry of Health has recently assumed responsibility for paying Regional and District Health teams**, funded by the Joint Health and Nutrition program (JHNP), and will need a payroll solution to be developed for these staff, possibly involving their incorporation into the FGS payroll. There is an estimated 3,741 health service delivery staff working in public facilities in southern Somalia as a whole (including Puntland and IJA).[9] This number – paid by a variety of NGOs and donor funds – comprises an estimated: 321 doctors; 169 pharmacists; 817 registered nurses; 65 registered midwives; 17 community midwives; and, 1,838 auxiliary nurses. The Ministry of Health estimates that between 30 to 40 percent of these personnel are entirely unpaid, and some are unqualified.

Fiscal Issues: Puntland

27. **The Government of Puntland has been facing serious fiscal challenges in 2012 and 2013, resulting in the accumulation of arrears**. The arrears are primarily in the form of unpaid salaries and allowances of public servants and unpaid bills to run day-to-day operations of the government. Although accurate accounting of arrears is not available, the stock of arrears as of December 2014 was estimated at about US$25.0 million (about 63 percent of total revenue).

28. **The Puntland government's revenues have been on an upward trajectory, albeit heavily reliant on taxes on international trade.** Since 2007, domestic revenues have increased by 92 percent from US$16.0 million to US$38.0 million, although that trend was reversed in 2013, with a decline of six percent. Most of the government revenues come from customs and related taxes on international trade, which contributed 67 percent of revenues in 2013. This lack of diversity makes revenues vulnerable to external shocks. An estimated US$8.0 million are collected in off-budget revenues.

29. **The rapid growth of the public sector payroll has presented a significant fiscal challenge for Puntland.** Despite the challenge of paying salaries and allowances of existing employees, the number of non-security public servants has increased by 47 percent since 2010 and 27 percent since 2012. The growth of security personnel was more dramatic at first, increasing 53 percent since 2010, but tapered later- increasing a modest 16 percent since 2012. The share of salaries and allowances of all public service employees in the total budget was 41 percent in 2010 and has since shown modest increases to 44 percent in 2013 and 47 percent in 2014.[10] The total salary budget increased by 55 percent between the original budget of 2011 and the 2014 revised budget, and 52 percent since 2013. The largest increase in the budget was between 2011 and 2012 when the total wage bill increased by 36 percent (34 percent for the non-security sector), while in 2013 the growth rate slowed down to 11 percent (4 percent in the non-security sector).[11] The changes in the wage bill are largely driven by the increase in the number of public servants. In March 2015, the government stopped the recruitment of new civil servants until salary arrears and other reform issues are addressed.

[10] Annualized number based on April-December budget.
[11] The wage bill for 2014 increased by only 2% and wage bill for non-security public servants is expected to decline by 8% despite the fact that number of non-security public servants has increased by 23%. This is further evidence of the poor quality of the data.

Table 3: Revenue and Expenditure Performance in Puntland

	2012		2013		2014	2015
Details/US$	**Budget**	**Actual**	**Budget**	**Actual**	**Budget**	**Budget**
On Budget - Total Domestic Revenue	***41.4***	***40.9***	***42.3***	***38.4***	***40.9***	***46,7***
Tax Revenue	33.8	31.8	37.2	32.4	***34.0***	***36.2***
Non-Tax Revenue	7.6	9.0	5.1	6.0	***6.7***	***6.7***
Surcharge					-	***3.8***
Off budget Revenue	-	***10.1***	-	***9.5***	-	-
Surcharge	-	8.2		8.4	-	-
remittance - Regional Accountants	0	0.7		0.0	-	-
Advances		1.2		1.1	-	-
Total Revenue and Grants	***41.4***	***51.0***	***42.3***	***47.9***	***40.9***	***46.7***
On budget - Total Expenditure	**41.4**	**42.4**	**42.3**	**52.5**	**40.9**	**46.7**
Salary	13.9	12.5	15.7	19.1	15.6	16.6
Allowance	2.8	2.6	3.2	4.2	3.5	3.5
Operations	24.6	27.3	23.4	29.2	21.8	26.6
Capital	-	-	-	-	-	-
Off budget Expenditure	**-**	**10.3**	**-**	**9.6**		
Surcharge Expenditure		8.2		8.4		
remittance - Regional Accountants		0.9		0.0		
Advances		1.2		1.1		
Total Expenditure	***41.4***	***52.7***	***42.3***	***62.1***	***40.9***	***46.7***
Surplus/(deficit)	**-**	**(1.7)**	**0**	**(14.3)**		

Source: Puntland Ministry of Finance.

Fiscal Issues: Interim Juba Administration (IJA)

30. **The IJA prepared its first ever six-month budget for the period July to December 2014.** This budget was based on total revenue and expenditures of US$7.6 million, of which 65 percent (US$4.9 million) was allocated to the Armed Forces, including US$4.6 million in wages and salaries. The new government is currently being established from scratch, and is therefore growing rapidly, with an estimated 394 civil servants and 4,895 non-civil servants (primarily the Jubbaland Security Force), envisaged by the end of 2015. The 2015 budget is for a total revenue of US$16.7 million- mostly made up of custom duties on imported goods, road taxes and fees. Compensation of employees represents 68 percent of recurrent costs but is mostly with respect to the police, Intelligence forces, prisons and political office holders.

Table 4: Revenue and Expenditure in IJA for 2014 and 2015

Details	2014 July to December US$ million	2015 January -December US$ million
Total Revenue	**3.1**	**16.7**
Tax	2.0	11.4
Non-tax rental income	0.1	0.8
Grants – FGS	1.0	2.2
Grants – International Org	0.0	2.3
Total Expenditure	**2.9**	**27.8**
Recurrent Expenditure	**2.8**	**16.7**
Compensations of employees	1.6	12.1
Use of goods & services	1.18	4.3
Grants (transfers to local government)	0.02	0.3
Capital expenditure	**0.1**	**11.1**
Balance	**0.3**	**11.1**

Source: Extract from IJA Ministry of Finance presentation and 2015 Appropriation Act

31. **At the macroeconomic level, the project aims to break the cycle of over-optimistic revenue projections, which are used to justify rapid growth in civil service payrolls that cannot be sustained**. In fact, the recent track record shows that despite strong revenue growth, albeit from a low base, fiscal space has, declined due to the increase in recurrent obligations and arrears. Under the project, along with related Public Financial Management (PFM) activities and policy dialogue, the government would face a well-defined revenue envelope, and strengthened budget formulation and financial management procedures would work to contain commitments within this envelope. At the same time, the financing of recurrent costs would be linked to the provision of critical human development services and the activation of rudimentary fiscal federalism. The experience of other fragile and conflict situations (e.g. Iraq) shows that without restraint on payroll expansion and associated building of PFM capabilities, states emerging from conflict will fail to build resilience to inevitable revenue volatility. This will imperil investments in state legitimacy once a subsequent revenue downturn is realized- with no buffers available to absorb it. At the minimum, fragile states need to limit arrears and establish a link between the size of the state and a sustainable revenue flow. These goals are embedded in the operation's design.

Payroll System

32. **FGS:** Until recently, monthly payroll processing involved ministries, departments and agencies (MDAs) submitting pay lists in hard copy to the Ministry of Finance. These submissions are subject to multiple manual checks, first by the Accountant General's Department against both the annual budget, and against a list of civil servants provided by the NCSC. The Auditor General's office also performs a check on these pay lists. Once checked, the Accountant General forwards the pay lists to the Central Bank of Somalia (CBS). The CBS is responsible for payroll execution, and provides a final check with civil servants required to present a photographic identification card and provide finger print identification through a biometric system to collect their monthly salary payment in cash at the CBS in Mogadishu.

33. **A number of incremental payroll and human resources reforms are planned and under implementation**. In 2014, the SFMIS was expanded to include a payroll module. This will help to automate the process within the Ministry of Finance (MoF), generating checks automatically and strengthening the payroll execution process. The February 2015 FGS payroll

was, for the first time, processed through the SFMIS payroll module- parallel to the established Excel-based approach. The Excel-based payroll system will be retired soon and the SFMIS will be used exclusively for payroll processing.

34. **The Puntland State** has a basic manual payroll and human resource management systems. Regional accountants are responsible for all receipts and disbursements through authorization by the MoF and Office of the Accountant General (OAG). The Chart of Accounts does not conform to the Government Financial Statistics Manual (GFSM 2001). There are also gaps in the payment mechanism. In some cases, authorized officials from some MDAs withdraw cash from the Puntland State Bank to pay salaries to employees and for goods and services from vendors.

35. **IJA,** with the assistance of the Somali Stability Fund (SSF) implemented BISAN Financial Management Information System (FMIS) to provide fundamental support to revenue and expenditure controls, help with budget execution and supervision, and to support overall fiscal discipline and enhance the efficiency and effectiveness of public revenue collection and expenditure. Currently, staff in five IJA entities receives stipend payments through the BISAN FMIS. Each Ministry or Agency submits a Payment of Salaries and Allowances request for the aggregate salary amount, with a pay list as an attachment, to the Treasury Department in the Ministry of Finance. The Treasury Department processes the aggregate payment to the Ministry official identified to receive the check. The cheque is then cashed with the Dahabshiil International Bank and the individuals identified are paid. This arrangement controls the aggregate amount of salary payments but does not provide measures to ensure that the list of payees is accurate, that staff have actually attended for work, or that they receive their full salary entitlement. A Civil Service Commission is being established and an improved payroll management system is being developed. This will lead to maintaining a permanent record and personnel files for all approved Civil Servants. Additionally, the FMIS is being enhanced to enable the recording of details of authorised Civil Service payees.

Inter-Governmental Fiscal Issues

36. **At present, revenues and expenditures are *de facto* highly devolved in Somalia, and *de jure* revenue and expenditure assignments are unclear.** Both the FGS and sub-national authorities collect all taxes simultaneously. In particular, most governments are heavily reliant on taxes collected at ports and airports (import, export and sales taxes), with these taxes accounting for 78 percent of FGS domestic revenues, 70 percent for Puntland (from imports and exports), and 48 percent for IJA in 2014. As a result, the FGS has one of the lowest domestic revenue to GDP ratios in the world at 1.7 percent (the Sub-Saharan average is 13.7 percent).

37. **There is some limited experience with inter-governmental fiscal transfers in Somalia.** The FGS made inter-governmental transfers totaling US$10.0 million in 2014. This was primarily channeled to the Banadir Regional Administration which receives 15 percent of Mogadishu port revenues- and a US$1.0 million transfer to IJA. Puntland and Somaliland have well established intra-governmental transfer systems, based on a categorization of districts from A-C, on the basis of size and capacity.

38. **Levels of public sector capacity and economic development are highly asymmetric across Somalia**. While Puntland has a well-established civil service and associated payroll and PFM systems, the newly emerging interim administrations in southern Somalia are in the process of setting up their governments. Likewise, given the fiscal reliance on port and airport revenues to finance public services, major disparities are likely to emerge between those sub

national entities that control ports on major trade routes and those that do not, meaning that fiscal equalization will become increasingly important for long-term cohesion.

C. Relationship to the Interim Strategy Note (ISN)

39. The ISN for FY14-16 was discussed by the World Bank Board on December 17, 2013 and aims to lay the foundations for poverty reduction and shared prosperity, delivering selected activities by: (i) strengthening core economic institutions; and, (ii**)** expanding economic opportunity. The project's focus on stabilizing the budget through salary payment and the establishment of a core payroll system that provides a financial and institutional platform for the Government corresponds with Strategic Objective I (Strengthening Core Economic Institutions) of the ISN.

40. **The** Recurrent Cost and Reform Financing Project (**RCRFP**) **Phase II project is one of the World Bank operations designed to address institutional governance issues through multiple approaches, over immediate and longer terms.** Somalia's governance challenges are complex and do not lend themselves to linear or singular approaches. The World Bank is addressing these challenges through a multi-nodal approach that includes fiscal support (recurrent costs), capacity injection, and core systems building and policy-dialogue. Implementation support will be coordinated under the Bank's Governance Global Practices and, as well, coordinated to the extent feasible, with other UN and donor engagements in the area through the Somalia Development and Reconstruction Facility (SDRF).

41. **This operation will provide one of several platforms for a stronger policy dialogue with the authorities on their macro-fiscal and economic governance track record.** As the World Bank reengages with Somalia through the MPF, and provides larger levels of financial support, the RCRF Phase II project will provide an opportunity to engage the Government in dialogue on its budget, especially as regards its non-military civil service wage bill and the priority of the Federal Government of Somalia (FGS) to, ultimately, fully finance these costs with its own domestic revenues, utilizing a realistic and balanced budget.

D. Situations in Urgent Need of Assistance or Capacity Constraints

42. Under the existing exceptional circumstances of conflict, security issues and acute institutional capacity constraints, pursuant to OP/BP 10.00, this project is being processed under provisions of paragraph 12 (Projects in Urgent Need of Assistance or Capacity Constraints) given the fragility and capacity constraints in the country. Somalia meets these requirements because: (i) it has experienced violent conflicts for the past twenty years; (ii) it is currently still experiencing conflict, with incessant bombings; and (iii) it is at risk of future violence. Additionally public revenue generation is still very low and severely constrained by on-going conflict, with significant under-performance relative to the 2014 budget. As reconstruction proceeds, the future expenditure needs of the government will increase. Failure to ensure a seamless transition of salary payments from the RCRFP Phase I project to RCRFP Phase II would undermine domestic and international confidence in the FGS. The SDRF will be the main source of funding over the next five years of implementation.

II. PROJECT DEVELOPMENT OBJECTIVE AND RESULTS

A. Higher-Level Objectives to Which the Program/Project Contributes

43. **The higher-level objectives are the same as for the RCRFP Phase I project and in keeping with operational guidance for a Series of Projects (SOP).** These objectives are as follows:

- Support macro-fiscal stability by providing **predictable financing** (salary payments and other recurrent costs for a given period) and **strengthened controls** for **expansion of social sectors,** especially education and health and the injection of high-capacity human resources;
- Increase **government legitimacy and credibility** through support of service delivery by center/regional government authorities and associated inter-governmental fiscal transfers;
- Support **institutional capacity-building** in human resources and provide a dialogue around human resource issues; and,
- Provide a **reliable financing mechanism** to allow government to have a financial buffer in case of unforeseen, but likely, internal and external shocks.

B. The Project Development Objective

44. **The Development Objective for the Series of Projects (SOP) is to enable the Somali Government to achieve reliable and transparent financing of critical civil service operations to help strengthen the legitimacy of the State**. The Development Objective of this second project *is to support the government to provide credible and sustainable payroll and to establish the foundation for efficient budget execution and payment systems for the non-security sectors in FGS and eligible federal member states, interim and emerging administrations.*

45. This aligns with the Multi Partner Fund (MPF) objective "to foster socio-economic recovery and stabilization by supporting the payment of civil service salaries, and the running costs of government institutions; financing technical assistance and supporting the building blocks of larger public investment programs across a range of sectors."

C. Project Beneficiaries

46. The main beneficiaries of the proposed project are: (a) the government, civil servants and employees of the implementing ministries, departments and agencies (MDA) in FGS, Puntland, IJA and other interim and emerging states; (b) the civil servants whose salaries would be covered under the project; (c) the Civil Service Commission that has the responsibility of providing the payroll; (d) social service workers (i.e., teachers and health workers in FGS, Puntland, IJA and other interim and emerging administrations); (e) citizens; and, (f) Development Partners who will have a convenient platform to provide technical advice and financial assistance.

D. Project Development Objective (PDO)-Level Indicators

47. The key PDO–level indicators of the project are as follows:

(a) *Credible payment to non-security civil servants, measured by:*

- The percentage of eligible civil servants' salaries in non-security sectors paid on time.
- The number of payroll verifications undertaken by independent agents.

(b) *Sustainable payment to non-security civil servant, measured by:*

- Share of the salaries of the non-security civil servants financed by the government.

(c) *Efficient budget execution and payment system to eligible interim and emerging states, measured by*:

- Percentage annual increase of inter-governmental transfers to sub-national governments.

E. Results Monitoring and Evaluation

48. **Progress in achieving the PDO will be measured and monitored through the indicators and intermediate results described in Annex 1**. The Annex provides details concerning reference data, targets, and frequency of data collection, including sources and methodology. A results framework, including monitoring, evaluation and reporting on progress and results, will be maintained by the External Affairs Fiduciary Section (EAFS) in FGS and in parallel units in Puntland and IJA (Annex 3) and in other eligible interim and emerging states. This arrangement will promote a high level of synergy and complementarities that will eliminate unnecessary duplication and promote program ownership by FGS and eligible federal member states, interim and emerging administrations.

III. PROJECT DESCRIPTION

A. The RCRF Program

49. **The project will be the fourth operation to be financed from the World Bank's MPF.** Both RCRFP Phase I and RCRFP Phase II are part of an approved wider RCRF "program" to be delivered through the SOP modality that allows for predictable financing within the framework of a macro-fiscal and reform-based dialogue between the Bank and the authorities.[12] The RCRFP Program aligns with the Government's policies and priorities and is prepared as a SOP, [13] using a condensed procedure and taking into consideration the need for

[12] "Investment Project Financing – Series of Projects Guidance Note," OPSPQ, April 9, 2013.

[13] Series of Projects: In cases of single-borrower sequential Projects, in addition to regular requirements, the documentation for the first Project presents the rationale for a phased approach, the potential benefits and risks of such an approach, the overarching DOs for the series, overall expected results, and a timeline for expected completion of each phase of the series; it also gives an indicative funding envelope for the entire series. Subsequently, each Project in the series is prepared and appraised individually, taking into account the performance to date of the preceding Project(s) in the series.

the client to make gradual improvements in capacity and overall performance. The Program focuses both on a short-term emergency operation designed to meet the urgent fiscal needs of the FGS, as well as a more sustained program of institutional reform and strengthening through follow-on projects. It is designed to support the government's agenda on core systems strengthening, through better budget execution, fiscal stability, and sound Public Financial Management (PFM). It is also designed as a platform for engagement and dialogue on core economic governance issues, including: (a) a strengthened fiscal and budgetary framework; (b) more reliable and effective service delivery (i.e. in education and health); (c) laying the foundations for an inter-governmental financing framework, with eligible interim administrations and federal member states (initially Puntland and IJA); (d) increased transparency in budget management- i.e., reliable, transparent and verifiable salary payment and HR systems, procurement, and PFM; and, (e) engagement with citizens by promoting greater public access to information.

50. **The first project in the series (RCRFP Phase I) financed and supported the development of an operational payroll and payment system at the Federal Government level for the non-security sector**, paid for salaries of existing non-security sector staff of the Federal Government, [14] and provided technical assistance and non-salary recurrent costs support to targeted departments in the FGS Ministries of Finance. This was intended to facilitate the strengthening of core government functions and basic service delivery, both of which are essential contributors to the increased relevance and legitimacy of Somali Government institutions.

51. **Strategic Approach*: There are important political and state building milestones in the state formation process that directs the context for RCRF II***. The elements of Somalia's future federation are emerging and there is increasing strategic importance to ensure that interim and emerging states are part of the broader fiscal and administrative discussions. This is a new and important factor in the context for development assistance in Somalia. The interim and emerging states will engage with RCRFP II on the basis of a series of 'Readiness Criteria' before receiving financing, as set out under Component 2 below. The readiness criteria will cover strategic; macro-fiscal; and PFM/administration and will be followed by an ongoing process of routine monitoring relative to an agreed set of benchmarks in subsequent years. The indicative allocations for 2016-2019 consequently reflect a gradual increase in the proportion of RCRFP II financing available for interim and emerging states in anticipation of this trend.

52. **The project will adopt a flexible approach to macro-fiscal dialogue through a series of annual reviews, timed to inform the various governments' budget preparation processes**. These annual reviews will: (i) agree on the following year's financial support; and, (ii) make any adjustments to the remaining project years. The output of the annual review process would be an agreed document between the government and the Bank on the specific allocation for each of the components and activities for the fiscal year.

53. **Macro-Fiscal Approach: The RCRF Phase II project represents a move away from gap-filling emergency support, towards a more developmental multi-year framework**. This framework aims to provide predictability and stability, while ensuring a flexible and effective platform for dialogue around macro-fiscal performance, strategic impact

[14] The following are considered core security actors and not eligible for financing under the project: armed forces; police; paramilitary forces; gendarmeries; presidential guards; intelligence and security forces; the coast guard; and customs authorities.

of the budget, and inter-governmental fiscal relations. The macro-fiscal dialogue would focus on issues such as the eligibility of expenditures at federal and regional government levels, and assessed revenue, expenditure, and PFM reform benchmarks. The project will contribute to macro-fiscal and budgetary stability and will support government's efforts at ensuring stability and sustainability including setting up (i) a public sector employment plan and a fiscally sustainable pathway for wages and salaries in relation to domestic revenues; and (ii) a balanced cash-based budget, based on a credible resource envelope, assessed by the World Bank in conjunction with the IMF to assess its fiscal dimension. In order to support the transition from RCRFP Project financing to domestic revenue financing of the wage bill, the Project will work with government and the PFM strengthening project on a revenue generation incentive activity from 2017 to support revenue policy and administration, within the existing resource envelope and as part of the annual review process.

B. Project Components

54. The Project has four components. A more detailed description of the project components and sub-components is given in **Annex 2**.

55. **Component 1: Support to core government functions of ministries, departments and agencies in FGS (US$81.0 million).** The Project will finance: the salaries of eligible non-security sector civil servants in the MDAs; the cost of staff injected under the capacity injection mechanism (CIM); and non-salary operating costs for MDAs.

56. ***Sub-Component 1:1: Financing of eligible civil service salaries in non-security sectors in Federal Government of Somalia (FGS) (US$49.0 million)****.* The Project would support the FGS to maintain core government functions during fiscal years 2015 to 2020. The project would finance the salaries of non-security sector civil servants at a cost of about US$48.0 million over the five-year project period. To underline the understanding that the government will ultimately finance all civil service salary payments from its domestic revenues, the project would finance these salary costs on a declining scale with the objective that these would be phased out by the end of the Project. The government would have to pay, on a timely basis, 100 percent of the salaries of the civil servants with the Project contributing an agreed proportion on a monthly basis. A detailed review of 100 percent of the government civil service salary expenditures will be carried out by the independent agent, confirming that the expenditures are eligible and meet agreed procurement and control procedures, including processing through the Somalia Financial Management Information System (SFMIS). From January 2016, payment of salaries to civil servants in the FGS is expected to be through their various bank accounts. The project will support the Central Bank of Somalia (CBS) in establishing the necessary payment systems and arrangements to facilitate this.

57. ***Sub-Component 1:2: Financing of salaries and allowances to government staff and young graduates recruited under the capacity injection mechanism (CIM) in FGS (US$17.0 million).*** The Project would finance the salaries and allowances of a cadre (525) of critical advisory, managerial and technical staff to fill urgent staffing gaps identified by the FGS through the CIM. This includes salaries and allowances of a number of young graduates who are expected to be absorbed into the civil service. All salary payments for government contracts will be made through the regular payroll process and directly to the bank accounts of the staff. Staff will be recruited through a central mechanism and at enhanced pay scales, on the basis of an agreed salary structure developed under the CIM. Recruitment will draw from a national, regional and diaspora candidate pool. Core government functions that will be strengthened under the CIM include: (i) policy and strategy management (planning, implementation and M&E); (ii) financial management (budgeting, accounting and auditing);

(iii) procurement management; (iv) revenue mobilization; and, (v) human resource management. Beneficiary institutions and eligible positions will be identified with the support of the World Bank and UNDP Capacity Injection Projects on the basis of agreed criteria.

58. ***Sub-Component 1:3: Financing of eligible non-salary recurrent costs in MDA in the FGS (US$15.0 million).*** The efficient operation of the MDA requires resources for non-salary operations costs; including, rent, petrol, oil and lubricants, repair and maintenance of vehicles and equipment, office materials, travel of civil servants, and utilities. In light of the pilot experience in four MDA under the RCRF Phase 1 project, where it was agreed that existing controls on these types of expenditures are weak, particularly in respect of confirmation of the actual expenditure incurred, the government established a task force to examine these issues and it has developed a new and updated set of processes and procedures for the procurement of these goods and services with appropriate financial management controls that ensure transparency, competition and accountability (**Annex 7**). All non-salary recurrent cost expenditures would be paid by the government and reimbursed by the Bank up to an agreed amount and for specific operating costs, based on a detailed review of 100 percent of these expenditures by the independent agent. The review will confirm that the expenditures are eligible, and that they have met agreed procurement and control procedures.

59. **Component 2: Inter-governmental fiscal transfers to core government functions of eligible federal member states, interim and emerging administrations (US$34.0 million).** RCRFP sub-national financing will reward accountable and transparent government in line with RCRFP broader principles**.** Interim and emerging states will need to comply with clearly defined readiness criteria before receiving financing. These criteria covers the following dimensions: (a) macro-fiscal, including fiscal, assessments; (b) PFM; (c) public administration; and, (d) social service delivery impact, (e) institutional and fiduciary capacity (see **Annex 2**.) It is expected that RCRF financing would be accompanied by matching funds for targeted service delivery expansion. The readiness criteria will be reviewed and updated on an annual basis to ensure adaptation to the rapidly evolving country context, and to manage the trade-off between the imperative of delivering expanded basic public services while also maintaining minimum fiscal and fiduciary management practices and systems in recipient governments. Essentially, the criteria will form the basis for inter-governmental fiscal transfers under the Project. At this stage, and on the basis of staff assessments and judgments, two regions have achieved a level of readiness for RCRF Phase II project support: i.e., Puntland and the IJA. Financing would be through an inter-governmental fiscal transfer, reflected in the FGS budget appropriation.[15]

60. ***Sub-Component 2:1: Transfers to interim and emerging states for core government functions (US33.0 million)***. The sub-component through the transfer grants from FGS to Puntland, IJA and other interim and emerging states will finance: (i) reforms to meet the readiness criteria; (ii) a pilot program of financing salaries and allowances of civil servants (excluding elected officials) in selected MDA; salaries and allowances to government staff and young graduates recruited under the CIM in interim and emerging states; (iii) systems-strengthening and the establishment of basic accountability systems; and, (iv) eligible non-salary recurrent costs for these selected MDA. Initially, allocations will be based on appraised needs, within the overall project resource envelope, although this approach to allocation will be subject to review over time and would evolve towards norm-based allocations with specific and developmental objectives. All payments will be made directly into the bank accounts of the respective staff or contractors.

[15] Although, it should be noted that, as an interim measure, funds flow may not initially be channeled through CBS in all cases until such time as CBS develops a functioning regional payment modality.

61. ***Sub-Component 2:2: Inter-governmental fora on transfers and information exchanges (US$1.0 million*).** As the constitutional framework and analytical basis are developed, the project will support government to lay the foundations for a simple system of inter-governmental dialogue, and associated resource transfers to strengthen inter-governmental trust, and, ultimately, of fiscal arrangements that promote greater equity in resource distribution among federal and sub-national governments. This will also finance technical assistance from FGS to support the interim and emerging states in inter-governmental relations.

62. **Component 3: Support of recurrent costs in health and education sectors in FGS and eligible member states, interim and emerging administrations *(US$20.0 million)***. The Project would support the FGS, Puntland and IJA to expand their service delivery systems through improvement of accountability systems and support of recurrent costs in the education and health sectors. The specific activities include financing: (i) the establishment of basic accountability systems in both sectors (US$1.5 million); (ii) eligible salaries and allowances for teachers and health workers from 2015 to 2020 (US$15.0 million); and, (iii) eligible non-salary recurrent costs in the sectors (US$0.5 million).

63. The Project will finance the salaries and allowances of eligible health workers and support the strengthening of the payroll system. **In the education sector,** in addition to financing the salaries of eligible teachers, deputy head teachers, head teachers, regional education officers (REOs) and district education officers (DEOs), the project will support efforts to strengthen the public education delivery system so as to address the issues of access, equity and quality in a sustained manner. **In Puntland,** the project will finance teachers, including head teachers. The project will also support incentive payments to a number of the DEOs and REOs. Based on defined criteria, these payments will be made ensuring that RCRF financing of salaries does not replace existing community, donor and government of Puntland financing of teacher salaries.

64. In addition, the Project will support implementation of some key systemic steps (including preparing a teacher recruitment, remuneration and career progression policy) in line with the Education Sector Strategic Plan (ESSP) linking the system strengthening with the financing of salary recurring costs. This will ensure that all new teachers be recruited based on criteria defined in the policy. Under the Project, technical assistance would also be provided to strengthen the Education Management Information System (EMIS) in interim and emerging states (Puntland and IJA), and some minimal hardware support may also be considered, depending on need. If required, technical support to develop and implement the teacher accountability framework will be financed under the Project.

65. **Component 4: Project management and coordination (US$9.0 million).** The component would support coordination, administration, communication, management, procurement, monitoring and evaluation (M&E), as well as impact-evaluation, auditing and dissemination of Project activities in FGS, Puntland and the IJA. It would finance dedicated staff to cover administration, financial management, procurement and communications. It would also support efforts to develop and strengthen the Fiduciary Sections of the Offices of Accountant General in FGS, Puntland, IJA and interim and emerging states through the financing of equipment, furniture and fittings, capacity-building, technical assistance, and other inputs as required. The Project would also support the Offices of the respective Auditor Generals with technical assistance to provide annual audits, and support the CBS with technical assistance to strengthen the payments systems.

66. The Project will undertake two impact evaluation (IE) studies. The first evaluation would look at ***Control Mechanisms for Non-salary Recurrent Expenses.*** Given the potential for misuse of these expenditures and the fact that existing controls of these types of expenditures are weak- despite new operational guidelines, including the use of an independent agent- the evaluation would examine whether pre-announcing audits by the MA would change the behavior of responsible officials. For some MDA, a high probability of an audit would be announced and a low probability, or nothing at all, would be announced for others, and the IE would observe and measure how different approaches influence mismanagement and corrupt behavior. The second study would cover the ***Linkages of pay to performance in the health and education sectors.*** The Project would support the development and implementation of accountability systems in both health and education, including the use of standard attendance sheets and enhanced supervision protocols. The IE will question whether or not these mandated checklists for health and education facilities differentiate performance, and, therefore, the quality of service delivery. The study will also look at how checklists for service delivery can be made more effective through the introduction of independent party monitors. Last, the IE would look at additional effects of capacity-building activities on administrators and inspectors and determine how to use supervisor check lists effectively.

C. Project Financing

67. The Project is prepared as an Investment Project Financing to be implemented by the FGS, and sub-national regional authorities and financed from the Somalia MPF that is administered by the International Development Association (IDA). The MPF operates in close partnership with government, donors and international agencies, within the context of the new Somalia Development and Reconstruction Facility (SDRF). Table 5 below shows total Project costs and financing (according to component and year), while Table 9 in Annex 2 indicates detailed total Project costs, disbursement percentages and the estimated amount of the MPF grant each Project year. It is based on the following assumptions: (a) salaries in FGS for civil servants are financed on a declining scale; (b) eligible expenditures for non-salary recurrent costs are reimbursed at 100 percent-up to a maximum allocated balance; (c) transfers from FGS to sub-regional authorities increase over the Project period; and (d) allocations and expenditures on social service delivery in education and health increase over the Project period.

68. The MPF Grant is US$144.0 million over a five-year period. MPF financing of the project has been confirmed at US$24.0 million for calender year 2015. Since the MPF must have donor cash deposits in hand before any Project commitments can be made, the allocations of US$30.0 million in 2016, 2017, 2018 and 2019 are indicative targets at this stage. Should these funds not be available at the required levels at the start of each project year, the allocations to each Project component would be reduced and the MPF grant agreement accordingly modified.

Table 5: Total Projects Costs and Financing

Component	Annual Amount of MPF Grant (US$ million)						Total Amount (US$ million)
	2015	2016	2017	2018	2019	2020	
			Indicative Amounts				
COMPONENT 1: Support to core government functions of MDAs in FGS.	16.0	18.0	18.0	16.0	13.0	0.0	81.0
COMPONENT 2: Inter-governmental fiscal transfers for core functions (grants from FGS to eligible federal member states, interim and emerging administrations).[16]	4.3	6.2	6.2	8.2	9.1	0.0	34.0
COMPONENT 3: Support of recurrent costs in health and education sectors in FGS and eligible federal member states, interim and emerging administrations.[17]	2.0	4.0	4.0	4.0	4.2	1.8	20.0
COMPONENT 4: Project management and coordination: Includes EAFS consultants; workshops, seminars, training, travel, communications, translation of documents, operational expenses, bank charges etc.	1.7	1.8	1.8	1.8	1.9	0.0	9.0
TOTAL	24.0	30.0	30.0	30.0	28.2	1.8	144.0

D. Lessons Learned and Reflected in the Project Design

69. The design of the RCRFP Phase I took into consideration lessons learnt from substantial international experience in supporting interventions in fragile and conflict-affected countries in Africa and in other regions of the world. These lessons are still relevant to the Phase II Project, and, in general, they indicate the need to keep project designs simple and to have clear fiscal sustainability plans; i.e., linking the amount of recurrent cost financing to clear revenue generation, expenditure controls, and budget management benchmarks.

70. The *Afghanistan Reconstruction Trust Fund (ARTF)* was established in 2002 and is still ongoing. That project has put in place a well-structured and regular salary-payment system that has a positive impact in supporting government reform processes and government legitimacy. Similar to what is planned under the RCRF Phase II, the ARTF demonstrates how budget and revenue generation targets can be a part of a broader dialogue of macro-fiscal performance and stability and can be an incentive to enhance project financing. There are similarities in Afghanistan and Somalia regarding the implementation challenges faced by different provinces. These challenges, and appropriate mitigation measures, were taken into

[16] The annual amounts of these transfer grants would have to be fully budgeted in FGSs Annual Approved Budget. For 2015, only US$3.0 million has been approved, hence a supplementary allocation would have to be approved by FGS before this component can be fully financed under the project.
[17] This component would be included in the approved annual budget of the FGS and transfers made to the appropriate sub-national authority.

account in regard to the differences in governmental reach and control in Mogadishu versus Puntland and IJA.

71. Similarly, The *Liberia Governance and Economic Management Assistance Program (GEMAP)* showed that, in a conflict country, it is crucial to protect the revenue streams of key revenue-generating agencies and institutions, as well as to secure revenues from customs duties, import levies, and taxes**.** This was accomplished in this project through a variety of means, such as: deploying international experts with binding co-signatory rights and authority to improve financial management system practices in selected institutions; and establishing escrow accounts for revenue generation. Revenue generation and collection is pertinent for the gradual reduction in financing of civil servants' salaries under this project and informs the proposed annual dialogue that is central to the project and the RCRF program in general.

72. Experience in the *Democratic Republic of Congo* reveals that outsourcing of implementation to technical partners, coupled with a clear exit strategy and the transfer of ownership to the Government, is an effective transition strategy in fragile states and helps to facilitate the achievement of "quick wins" during implementation. In the Somali context, this "outsourcing" experience is seen in the role played by Somali Subject Matter Experts (SMEs) who are consultants drawn mainly from the Somali Diaspora and bring with them extensive technical and professional knowledge from abroad, coupled with a deep understanding of the socio-political context of the country. Clearly these SMEs have already provided the FGS with some quick wins in establishing core functions in MDA under the RCRF Phase I Project. Finding effective ways for SMEs to transfer their knowledge to Somali civil servants in Puntland and the IJA, and providing appropriate incentives to retain the SMEs in service for longer periods of time, is a strategic priority and objective that has been factored into this Phase II Project and other MPF-funded projects.

73. Last, the *Sierra Leone Pay and Performance Project* supported three reform areas: pay reform; recruitment and staffing; and, performance management. It also financed civil servants' salaries, according to the pay structure. The most important lesson learned is that recurrent salary support from the World Bank and donors to a country must be accompanied by the recipient government's commitment to salary-payment system reform (including civil service recruitment, staffing and performance). The linkages between the RCRF Project and the PFM, Capacity Injection, and other projects (see below) confirm that these lessons have been internalized and used in the design of the operation.

74. **The RCRFP Phase I Project is rated satisfactory, both in terms of the achievement of development objective and the implementation progress.** All Project funds of US$16 million are almost fully disbursed and all Project activities are fully implemented. The phase II Project will address the challenges encountered by the Special Financing Facility (SFF) and RCRFP Phase I projects. A detailed description of the Phase I Project Performance and Experience is given in **Annex 6**.

E. Linkages with other Projects in Somalia

75. This project is linked to the on-going World Bank/MPF-financed *Public Financial Management Capacity Strengthening Project (PFMCSP) and the Public Sector Capacity Injection Project (CIP)*. The two projects are establishing controls that are critical in supporting the control and payment processes for the RCRFP Project. The PFMCSP will establish the PFM fundamentals to underpin the RCRFP and provide the much-needed technical assistance for the Federal Government to meet the PFM commitments of the

Financial Governance Program. The scale-up project under preparation involves the upgrade of the payroll module of the SFMIS web-based technology in order to support the transfer of payroll responsibilities from the CBS to the Accountant General's department. The SFMIS includes a framework for the Human Resource Management (HRM) module that will inform payroll calculations and, subsequently, a common platform for the HRM-Payroll. The National Civil Service Commission (NCSC) will establish a comprehensive employee HR database that will be linked to the payroll, building on the biometric verification currently being done by the CBS. This would involve payment instructions to CBS to transfer funds to the regulated commercial banking institutions to directly pay government workers, instead of the current situation in which civil servants queue at the CBS to collect their salaries.

76. The CIP will recruit Somali diaspora advisors, young graduates and managers into the civil service, based on the recruitment policies, systems, guidelines, terms of reference and job descriptions developed under the PFMCSP. It will also put in place credible data to support payment of salaries under the RCRFP, based on harmonized salaries and allowances.

77. **The World Bank and IMF are leading in engaging the CBS in its payment system and banking arrangements**. These include support in establishing and finalizing correspondent banking arrangements and relations with foreign financial institutions and due diligence of respective financial institutions. In addition, the World Bank is supporting the development of the FGC- a partnership between the FGS, MoF, CBS, and Office of the President- and international financial institutions (i.e., the AFDB [African Development Bank], World Bank and IMF- participating as an observer) to provide enhanced oversight of FGS concessions and procurement, CBS strengthening, PFM reform, and the development of adequate partnering in these areas. **Figure 2** is a governance results chain which shows the linkages between the outcomes of the proposed project and other projects being supported by the World Bank.

78. **The Project also engages with projects and programs supported by other Development Partners**. The European Union (EU) has just completed an assessment of the HR and payroll systems in Somalia. The NCSC, through support from other development partners, is developing policies and procedures for maintaining establishment information with pre-defined compensation entitlements (grade/pay and allowances), and this will further strengthen payroll controls and ensure consistency between the nominal roll and the payroll.

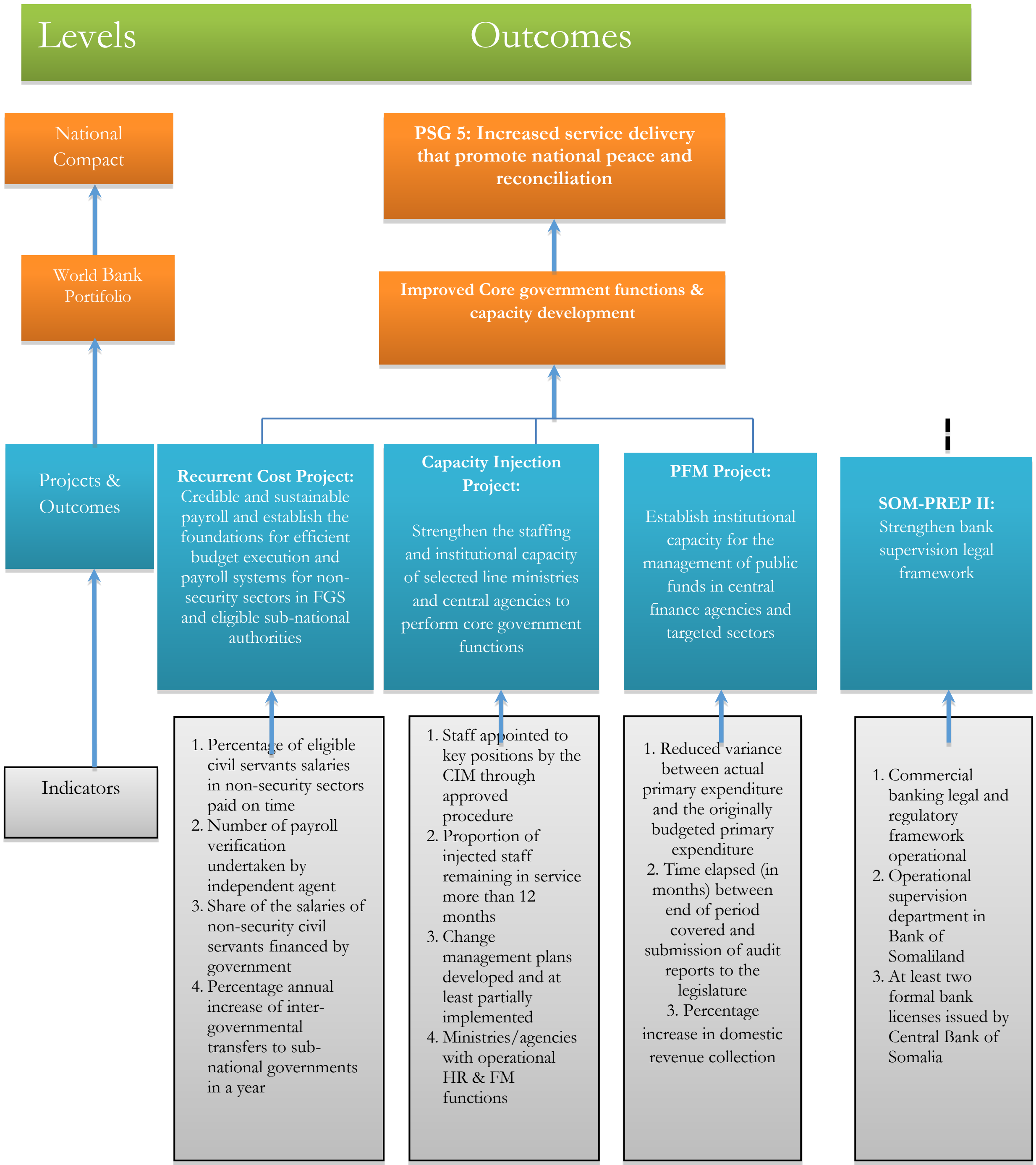


Figure 2: Somali Governance Results Chain

IV. IMPLEMENTATION

A. Institutional and Implementation Arrangements

79. **The RCRF Phase II Project implementation arrangements.** The FGS will provide strategic direction with respect to policy and financing. To avoid an overly complex structure and to lower transaction costs, the Project will use existing aid coordination architecture under

the SDRF. The proposed governance arrangements will consist of a Project Steering Committee, a Project Management Team and a PFM Reform Coordination Unit, which would work closely with the EAFS team in the Offices of the Accountant General for project implementation. An EAFS team would support implementation in the FGS and Puntland and subsequently in IJA and other sub-national entities as they are established and join the Project. The Project would leverage the SSF, supported by multi donors, to pilot IJA salaries in year 1. An independent agent is being engaged under the MPF umbrella. The FGS will engage a project coordinator while each participating interim and emerging states will engage a project manager that will be responsible for implementation in their entity. Implementation arrangements for interim and emerging states will be updated when the authorities come into existence and are included in the project. The details of Project implementation organizational arrangements, agreed financial management and procurement processes and procedures- including the Flow of Funds- are outlined in **Annex 3.** An Implementation Strategy and Action Plan is given in **Annex 5**.

V. KEY RISKS AND MITIGATION MEASURES

A. Risk Rating Summary

80. A full Systematic Operations Risk-rating Tool (SORT) is outlined in **Annex 4.** A Summary is presented below.

Table 6: Summary SORT Assessment

	Risk Category	**Rating**
1.	Political and governance	Substantial
2.	Macroeconomic	High
3.	Sector Strategies and Policies	Substantial
4.	Technical design of project or program	Substantial
5.	Institutional capacity for implementation and sustainability	Substantial
6.	Fiduciary	High
7.	Environment and social	Low
8.	Stakeholders	Substantial
9.	Others (security)	High
10.	**Overall Implementation Risk**	**High**

B. Overall Risk Rating Explanation

81. **The overall risk rating for the Project is high**. Somalia is a high-risk environment and careful management of risks is required. Major country risks include bad governance and corruption, the volatile security situation, incessant instability because of an active insurgency led by Al-Shabab, and weak capacity to manage projects. This could have a number of direct

and indirect impacts on the program, ranging from periodic travel restrictions to a direct attack by Al-Shabab on Government institutions, including the CBS- the primary pay-point for civil servants. Given the declining scale of project funding of salaries, the sustainability of salary payments and full takeover by the end of the Project is a major risk. The program will mitigate these risks by taking account of regular security advice issued by the World Bank and UN, and by relying heavily on the more flexible security arrangements and access arrangements by the independent agent engaged for all MPF projects to ensure that implementation can continue when staff travel is restricted. The project will also rely on the security measures that the FGS has taken to protect the CBS and other core PFM institutions from attack. An early mid-term review, after eighteen months of implementation, will include budget, revenue and inter-governmental fiscal discussions to assess the sustainability of salary payments by the government.

VI. APPRAISAL SUMMARY

A. Economic and Financial Analysis

82. **The usual economic and financial analysis for this Project was not carried out, given the paucity of economic data, the ongoing conflict and fragility in southern Somalia, and the uncertainty in determining costs and benefits**. However, the implementation of the Project would increase the legitimacy and functionality of the State and bring benefits to the public. The payment of salaries and support of expenditures in the social sectors, particularly health and education, is an essential precondition for the restoration of public confidence in the legitimacy of state structures and could support a peaceful State, with security dividends resulting from the improved fiscal position of recipient governments. This will also reduce the accumulation of State financial obligations, particularly arrears that are a fiscal challenge for the FGS and regional governments. Leveraging the lessons from implementation of the Project, Phase I – which has been incorporated in the current design, - the impact is likely to further enhance State legitimacy. More so, an impact evaluation will be conducted to assess improved social service performance, and will provide the foundation for strengthening service delivery systems.

83. **Sustainability and restoration of key economic institutions will be essential for growth and development in Somalia**. **The long-term challenge for all recurrent financing instruments is the Government's own fiscal sustainability**. The Government has stated the policy goal of financing existing recurrent costs (reflected in the 2014 budget), or 'core costs,' entirely from domestic resources as soon as feasible. The Project supports: regular discussion of the budget, prioritization, revenue generation and expenditure controls; a forum for dialogue with the regions on the readiness criteria for inter-governmental fiscal transfers; payroll and payments systems reforms; and, the development of the CBS's proper role as fiscal and financial agent to the FGS, supporting the transition of payroll execution within the CBS to payroll execution within the Ministry of Finance.

B. Technical Evaluation

84. **The Project is an integral part of the World Bank and donor community response to the government's urgent need to foster socio-economic recovery and stabilization**. It will do this by supporting the payment of civil service salaries and the running costs of government institutions, and financing technical assistance. The Project is based on a simple technical design, which takes into account the country's weak capacity and the right balance between rapid results (payment of salaries of non-security staff for the establishment of public

services) and medium-term objectives to ensure sustainability. The technical design includes an internal control framework to institute controls in payments of salaries and non-salary recurrent cost expenditures in the civil service.

C. Financial Management

85. **The financial management risk is assessed as High**. This is confirmed in the JNA-RDP and the PFM Needs Assessment which recognizes that systems managing public resources are very weak with a rudimentary, unregulated banking sector, high potential for money-laundering and vulnerability to acts of financial and other kinds of terrorism. In addition, there is the potential of restricted movement, high insecurity and volatility due to active Al-Shabaab-led insurgency. While recognizing this, the Bank will work closely with the government to support and strengthen the Use of Country Systems (UCS) without creating parallel arrangements and in line with the provisions of the "Somalia New Deal". The FM arrangements will be continuously monitored through frequent FM supervisions and independent monitoring, and will be updated to reflect the emerging developments in the FM systems. A detailed description of the project financial management system and flow of funds arrangements are detailed in **Annex 3.**

D. Procurement

86. **The procurement risk is assessed as high**. Procurement for the Project will be carried out in accordance with the EAFS Operational Manual and the latest revision of the World Bank Procurement Guidelines. The detailed procurement assessment is given in **Annex 3** and includes a simplified procurement plan for Project implementation.

E. Social Impact (including Safeguards)

87. **The timely payment of civil servant salaries supported by this Project is expected to have a positive social impact**. Phase I directly benefited up to 4,000 households in and around the Benadir region of southern Somalia. This Phase II Project will extend those benefits to other regions and Federal Member States (Puntland and IJA). Additionally, the support to non-recurrent cost expenditures in the health and education sectors will support service delivery and have a positive social impact on the populace.

F. Environmental Impact (including Safeguards)

88. **The activities supported by the Project will have no adverse environmental impacts**. The Project is therefore classified as Environmental Category C. No specific environmental safeguard instrument will be required. Consequently, World Bank policies in this area are not triggered.

G. World Bank Grievance Redress

89. Communities and individuals who believe that they are adversely affected by a World Bank (WB)-supported project may submit complaints to existing project-level grievance redress mechanisms or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address project-related concerns. Project-affected communities and individuals may submit their complaints to the WB's independent Inspection Panel that determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at

any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate GRS, please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

SOMALIA: Recurrent Cost and Reform Financing Project: Phase II

Annex 1: Results Framework and Monitoring

	Project Development Objectives												
	The Development Objective of the project is to support the government to provide credible and sustainable payroll and to establish the foundation for efficient budget execution and payment systems for the non-security sectors in FGS and eligible federal member states, interim and emerging administrations.												
	Project Development Objective Indicators												
					Target Values						**Frequency**	**Data Source/ Methodology**	**Responsibility for Data Collection**
Indicator Name	Core	Unit of Measure	Baseline	2016	2017	2018	2019	2020	End Target				
1. Percentage of eligible civil servants' salaries in non-security sectors paid on time[18]	☐	Percentage	0	30	50	70	80	80	80	Monthly	Progress Report and MA Advisory Report	EAFS/Office of Accountant General; Independent agent
2. Number of payroll verifications undertaken by independent agent		Number	6	10	14	18	22	26	26	Quarterly	Progress Report and MA Advisory Report	EAFS/Office of Accountant General; Independent agent
3. The share of the salaries of the non-security civil servants financed by the government		Percentage	0	30	40	60	80	100	100	Annual	Government Budget, Progress Report and MA Advisory Report	EAFS/Office of Accountant General; independent agent
4. Percentage annual increase of inter-governmental transfers to sub-national governments		Percentage	0	10	20	20	40	50	50	Annual	Government Budget, Progress Report and MA Advisory Report	EAFS/Office of Accountant General; independent agent

[18] Paid on time means ready for payment with the CBS or the commercial bank between the government statutory pay period of 25th and 30th of the month

	Intermediate Results Indicators											
Indicator Name	Core			**Cumulative Target Values**							**Data Source/**	**Responsibility for**
	☐	**Unit of Measure**	Baseline	2016	2017	2018	2019	2020	End Target	**Frequency**	**Methodology**	**Data Collection**
5. Number of monthly payroll reports published on MoF website		Number	4	12	12	12	12	12	12	Monthly	Progress Report and MA Advisory Report	EAFS and Independent agent
6. Establishment of payment systems by the Central Bank of Somalia/ Dahabshiil International Bank		Yes/No	No	Yes	Yes	Yes	Yes	Yes	Yes	Bi-Annual	Progress Report, Central Bank of Somalia	Central Bank of Somalia/EASF/Office of Accountant General
7. Verified reimbursements of non-salary recurrent cost expenditures		Number	0	12	12	12	12	12	60	Monthly	Progress Report, MA Advisory Report; MoF website	EAFS and independent agent
8. Number of annual inter-governmental fiscal transfer dialogues held		Number	0	3	3	3	3	1	13	Quarterly	Progress Report	EAFS and Office of Accountant General
9. Fully functional EMIS with integrated teacher profile and HR System		Yes/No	No	IT-based payroll system adopted	Teacher recruitment policy developed	Teachers recruited under new policy	Yes	Yes	Yes	Annual	Progress report	MoE

Somalia: Recurrent Cost and Reform Financing Project: Phase II

Annex 2: Detailed Project Description

1. The project has four components

2. **Component 1: Support to core government functions in MDA of FGS (US$81.0 million).** The Project will finance: (i) salaries of eligible non-security-sector civil servants in the MDA, including teachers and health sector workers; (ii) the cost of staff injected under the capacity injection mechanism (CIM); and, (iii) non-salary operating costs for MDA.

3. ***Sub-Component 1:1: Financing of eligible civil service salaries in non-security sectors in FGS (US$49.0 million)***. The Project would finance the salaries of non-security-sector civil servants on a declining scale over the project implementation period, with the objective that these would be phased out by the end of the Project when the government will ultimately finance all civil service salary payments from its domestic revenues. The independent agent will carry out a detailed review of 100 percent of the government civil service salary expenditures confirming that expenditures are eligible and meet agreed procurement and control procedures—including, processing through the SFMIS. Any ineligible salary payment will be reduced from the Project's contribution for the month. From January 2016, payment of salaries to the civil servants is expected to be through their various bank accounts. The project will support the CBS in establishing the necessary payment systems and arrangements to facilitate this process.

4. ***Sub-Component 1:2: Financing of salaries and allowances to government staff and young graduates recruited under the CIM in FGS (US$17.0 million).*** The Project would finance the salaries and allowances of a cadre of critical advisory, managerial and technical staff to fill urgent staffing gaps identified by the FGS through the CIM. It will also pay salaries and allowances of a number of young graduates who are expected to be absorbed into the civil service. All salary payments for government contracts will be made through the regular payroll process. Staff will be recruited through a central mechanism and at enhanced pay scales on the basis of an agreed salary structure developed under the CIM. Recruitment will draw from national, regional and diaspora sources. Core government functions that will be strengthened include: (i) policy and strategy management (planning, implementation and M&E); (ii) financial management (budgeting, accounting and auditing); (iii) procurement management; (iv) revenue mobilization; and (v) human resource management. Beneficiary institutions and eligible positions will be identified with support of the World Bank and UNDP Capacity Injection Projects on the basis of agreed criteria.

5. In the FGS, the estimated number of government staff and young graduates to be financed over the course of five years is expected to be 525 and their estimated salaries would cost US$17.0 million over five years. These include 15 senior advisers, 30 technical advisers, 30 senior managers, 75 middle level management staff and 375 young graduates. Table 3 below shows the number and projected salary and allowance costs for government staff and young graduates under the CIM.

Table 7: Projected Annual and Total Salary and Allowance Costs for Staff recruited through the Capacity Injection Mechanism over the Five-year Project Period

	Total number of staff & young graduates recruited under CIM	Estimated Annual Salary Costs US$					Projected Total Salary costs for five years
		Year 1	Year 2	Year 3	Year 4	Year 5	
FGS	525	2,000,000	4,000,000	5,000,000	4,000,000	2,000,000	17,000,000

6. ***Sub-Component 1:3: Financing of eligible non-salary recurrent costs for MDA in the FGS (US$15.0 million).*** The efficient operation of the MDA requires resources for non-salary operations costs, including rent, petrol, oil and lubricants, repair and maintenance of vehicles and equipment, office materials, travel of civil servants, and utilities. The existing controls on these types of expenditure are weak, particularly in respect to confirmation of actual expenditures incurred. A government Task Force has developed processes and procedures for the procurement of these goods and services with appropriate financial management and payment controls that ensure transparency, competition and accountability (Annex 7). All non-salary recurrent cost expenditures would be paid by the government and reimbursed every two months by the Bank, based on a detailed review of 100 percent of these expenditures by the independent agent, confirmation that the expenditures are eligible, and that they have met agreed procurement and control procedures.

7. **Component 2: Inter-governmental fiscal transfers for core government functions in eligible federal member states, interim and emerging administrations (US$34.0 million).** RCRFP sub-national financing will reward accountable and transparent government in line with RCRFP broader principles and would be through an inter-governmental fiscal transfer, reflected in the FGS budget appropriation**.** Regions and federal member states will need to comply with clearly defined readiness criteria before receiving financing. These criteria cover the following dimensions: (a) macro-fiscal, including fiscal, assessments; (b) PFM; (c) public administration; and, (d) social service delivery impact. Table 4 below outlines the criteria. It is expected that RCRFP financing would be accompanied by matching funds for targeted service delivery expansion. The readiness criteria will be based on consultations with FGS and eligible federal member states, interim and emerging administrations, and will be updated on an annual basis to ensure that states adapt to the rapidly evolving country context, and to manage the trade-off between the urgent imperative to deliver expanded basic public services while also maintaining minimum fiscal and fiduciary management practices and systems in recipient governments. Essentially, the criteria form the basis for inter-governmental fiscal transfer under the project.

Table 8: **Proposed Dimensions, Challenges and Objectives for Readiness Criteria**

Dimension	Challenge	Objective
Macro-fiscal	Low revenues, unrealistic revenue projections, poor budget credibility, poor budget transparency resulting in ineffective public spending	Track and support a dialogue on improvements in revenue mobilization, macro-fiscal management, PFM and administrative management
Public finance management	Weak systems for payroll and operating expenditures resulting in inefficient public spending	Support the development of effective systems with robust controls for civil service salary payment and operating expenditures
Public administration	Very new interim administrations lack basic functions, limiting their credibility	Support the establishment of core civil service functions (i.e. newly established interim administrations)
Social service delivery impact	Limited frontline social service delivery by public sector, resulting in poor social outcomes	Support the incremental expansion of social service provision at subnational level where appropriate capacity exists (i.e. more mature Federal Member States)

8. ***Sub-Component 2:1: Transfers to interim and emerging states for core government functions (US$33.0 million).*** This will support core government functions in the Puntland State, IJA and other interim and emerging states (including Interim Southwest Administration, Interim Central States Administration, and the Interim South Central East Administration), based on meeting the eligibility criteria as detailed in annex 7. The Project, through the transfer grant from FGS to Puntland, IJA and other interim and emerging states (as they emerge), will finance: (i) reforms to meet readiness criteria; (ii) a pilot program to finance eligible non-military civil service salaries in selected MDA; (iii) salaries and allowances to government staff and young graduates recruited under the Capacity Injection Mechanism (CIM) in interim and emerging states; and (iv) non-salary recurrent costs for these selected MDA. Initially, allocations will be based on appraised needs, within the overall project resource envelope, although this approach to allocation will be subject to review over time and would evolve towards norm-based allocations with specific and developmental objectives. All payments will be made directly into the bank accounts of the respective staff or contractors.

9. ***Sub-Component 2:2: Inter-governmental fora on transfers and information exchange (US$1.0 million*****).** As the constitutional framework and analytical basis are developed, the project will support government to lay the foundations for a simple system of inter-governmental dialogue, and associated resource transfers, to strengthen inter-governmental trust, and, ultimately, fiscal arrangements that promote greater equity in resource distribution among federal and sub-national governments. This will also finance technical assistance to support the interim and emerging states in meeting the readiness criteria. The annual framework will be agreed in August or September of each year before the start of the next financial year. Indicative annual policy dialogue would focus on financing salary expenditures, revenue targets, policy initiatives, payroll ceilings, recurrent expenditure norms, operations and management expenditures, and third party monitoring.

10. **Component 3: Support to recurrent cost in education and health sectors in FGS and eligible federal member states, interim and emerging administrations (Puntland and IJA) (US$20.0 million*)*.** The Project would finance technical assistance to support the efforts of FGS and Puntland and IJA to expand their service delivery systems, especially in the education and health sectors. This is in line with the formal request from the FGS seeking World Bank support for civil service salaries in other regions and sectors, including health and education. RCRFP I included financing to support technical assistance to the FGS to identify and prepare estimates for support under

RCRFP II to Puntland and IJA and for the health and education sectors. The Project would finance: (i) setting up basic accountability systems in both sectors in year 1 (US$1.5 million); (ii) salaries and allowances for eligible teachers and health workers (US$15.0 million); and (iii) eligible non-salary recurrent costs in the sectors (US$4.5 million).

11. A review of the current HR, payroll and recurrent cost mechanisms used by the Federal Ministries of Education and Health and the sector authorities in Puntland State of Somalia and the IJA has been carried out. The consultants reviewed the arrangements by non-state actors, such as NGOs and UN agencies, for funding service delivery staff.

12. The consultant's analysis resulted in three concrete deliverables: (i) an assessment report covering existing payroll systems, information gaps and recurrent costs for the Ministries of Health across the FGS, Puntland and the IJA; (ii) a cost estimate and detailed work plan, based on the above mentioned report, outlining steps towards the establishment of a payroll system linked to the national budget, agreed by both the Ministries of Health and the Federal Ministry of Finance; and (iii) further development of relevant IT tools, specifically the HRIS database already in use for several FGS Ministries, in order to prepare them for subsequent roll-out across the Ministries and sectors.

13. While the Project will finance the salaries of the eligible civil servants in the education sector, particularly teachers, deputy head teachers, head teachers, regional education officers and district education officers, the Bank will ensure that Project financing neither substitutes nor makes double payment to any of these education civil servants, as many teachers and other education officers are already paid by the donors; e.g., those paid by the UNICEF-managed GPE Project, EU-funded projects, and others. The FGS, Puntland and IJA will provide complete lists of education civil servants, particularly those working in basic/primary education and secondary education sub-sectors. All the zones seem to have prepared teachers' profiles, which need to be updated with current information. In addition to the HR payroll, all the beneficiary zones will update teacher profiles. A sample-based verification will be conducted to validate the profiles.

14. In order to strengthen the public education delivery system to address issues of access, equity and quality in a sustained manner, it is critical to link the financing of salary-recurring costs to some minimum systemic steps; these are: in year one (2015) the FGS, Puntland and IJA need to prepare a teacher recruitment, remuneration and career progression policy with all necessary approvals so that in year two of the Project (2016), these can be implemented. This will ensure that all the new teachers recruited in year two and afterwards are recruited based on the criteria defined in the policy. FGS and Puntland have established an EMIS at the Ministry of Education. However, the EMIS is not optimally functional. Under the Project, technical assistance will be provided to strengthen the EMIS, and some minimal hardware support may also be considered, depending on need. While ensuring that the teachers and education civil service cadre at regional and district levels are paid regularly, based on a payroll system, it is important to develop a basic teacher accountability framework linking the payment of salary to performance. Under on-going donor-funded projects, each zone has some kind of teacher accountability system. The zones will be encouraged to build on the existing teacher accountability mechanism and share it with the Bank in year two of the project (2016), and upon the Bank's acceptance of the mechanism, each zone with start implementing it from year three (2017). If required, technical support to develop and implement the teacher accountability framework will be financed under the Project. In a nutshell, payment of education civil servants at school, regional and district levels in year one will be contingent upon the updating of teacher profiles; and, in year two, development of teachers' recruitment, remuneration and career progression policy and EMIS; and, in year three, would be contingent upon the development and implementation of a teachers' accountability framework.

15. Based on the analysis of the consultants, the project will support FGS, Puntland and the IJA to strengthen health personnel payroll systems in concert with the joint efforts of the Ministry of Health and Ministry of Finance. This strengthening will be coordinated with national and state-wide payroll system reforms, with an emphasis on the unique characteristics of the health sectors. A work plan to strengthen the payroll system will be developed to fill information gaps, make necessary changes, link with an accountability system, and improve existing IT tools; e.g., the HRIS database. It is expected that implementation of the work plan will start from year two (2016).

16. **The Project will also provide support for FGS, Puntland and IJA to improve their accountability systems in the health sectors**. Evidence shows that attendance sheets for health personnel are not well linked to the existing payroll system, thus separating salary payment from service delivery. Consequently, health workers may be absent from work in order to earn extra income in private practice or simply to increase their leisure time. For this and other reasons, it is therefore important to enhance supervision by administrators and inspectors employed by third parties (such as independent organizations or communities). There will be three specific guidelines for this supervision:

- A supervision checklist tool will be developed for regular use by administrators at all levels, including the Ministry of Health, regional health offices and district health offices,[19] in order to monitor service delivery to respective areas, monitoring the presence of qualified staff and service delivery and record keeping, attendance sheets, availability of basic supplies, and the general hygiene situation.
- An independent party will be identified to visit health facilities unexpectedly once per quarter and inspect selected items on the checklist. Subject to the readiness of the Government, a pilot or phase-in approach will be used to start in selected districts.
- Capacity-building activities will be undertaken for administrators and inspectors to learn how to use the supervision checklist.

17. **Component 4: Project management and coordination in FGS, Puntland and IJA (US$9.0 million).** This component would support the coordination, administration, communication, management, procurement, monitoring and evaluation (M&E), audit and dissemination of Project activities in FGS, Puntland and the IJA. It would finance dedicated staff to cover project coordination and management, administration, M&E (including impact evaluation), financial management, procurement and communications. It would also support efforts to develop and strengthen the fiduciary sections of the Offices of Accountant General in FGS, Puntland and IJA regional governments through the financing of equipment, furniture and fittings, capacity-building, technical assistance, non-salary recurrent costs, and other inputs as required. The project would also support the offices of the respective auditors general with technical assistance to provide annual audits during the project implementation period.

18. **Table 5** indicates detailed total Project costs, disbursement percentages and the estimated amount of the MPF grant each Project year. It is based on the following assumptions: (a) salaries in FGS for civil servants are financed on a declining scale; (b) eligible expenditures for non-salary recurrent costs are reimbursed at 100 percent up to a maximum allocated balance; (c) transfers from

[19] It is assumed that undertaking regular supervision will be part of administrators' routine work. Therefore, regular supervision per se is not considered part of project activities and will not generate any extra cost. This is considered reasonable, as their salaries have been paid through project component 1. The project will support the development of the tool for supervision. Whether independent inspectors will impose any extra costs depends on whether it will be government agencies or communities/NGOs that do the inspecting. Extra costs may be needed if communities/NGOs are identified for the task.

FGS to sub-regional authorities increase over the project period; and, (d) the allocations and expenditures on social service delivery in education and health increase over the project period.

19. The MPF Grant is US$144.0 million over the five-year period. MPF financing of the project has been confirmed at US$24.0 million for 2015 calendar year. Since the MPF must have donor cash deposits in hand before any project commitments can be made, the allocations of US$30.0 million in 2016, 2017, 2018 and 2019 are indicative targets at this stage. Should these funds not be available at the required levels at the start of each Project year, the allocations to each Project component would be reduced and the MPF grant agreement accordingly modified.

Table 9: Total Project Costs and Financing

Component	Annual Amount of MPF Grant (US$' million)						Total Amount (US$'million)
	2015	**2016**	**2017**	**2018**	**2019**	**2020**	
Component 1: Support to core government functions of MDAs in FGS		Indicative amounts					
Sub-Component 1.1: Financing eligible civil service salaries in the non-security sectors in FGS	13.0	12.0	10.0	8.0	6.0	0.0	**49.0**
Sub-Component 1.2: Financing salaries and allowances for government staff and young graduates recruited under the Capacity Injection Mechanism in FGS	2.0	4.0	5.0	4.0	2.0	0.0	**17.0**
Sub-Component 1.3: Financing of eligible non-salary recurrent costs for MDA in FGS for MDA	1.0	2.0	3.0	4.0	5.0	0.0	**15.0**
SUB-TOTAL COMPONENT 1	**16.0**	**18.0**	**18.0**	**16.0**	**13.0**	**0.00**	**81.0**
Component 2: Inter-governmental fiscal transfers for core functions (Grants from FGS to eligible federal member states, interim and emerging administrations[20]							
Sub-Component 2:1: Transfers to interim and emerging states for core government functions Grant based on financing: (i) in Year 1 of project, reforms to meet readiness criteria; (ii) pilot **financing of eligible non-military civil service salaries in selected MDA**; and (iii) **non-military recurrent costs of selected MDAs**	4.0	6.0	6.0	8.0	9.0	0.0	**33.0**
Sub-Component 2.2: Inter-governmental fora on transfers and information exchange	0.3	0.2	0.2	0.2	0.1	0.0	**1.0**
SUB-TOTAL for COMPONENT 2	**4.3**	**6.2**	**6.2**	**8.2**	**9.1**	**0.0**	**34.0**
Component 3: Support of recurrent costs in health and education sectors in FGS and eligible federal member states, interim and emerging administrations[21]							
Sub-Component 3.1: Setting up basic accountability systems	1.5	0.0	0.0	0.0	0.0	0.0	**1.5**
Sub-Component 3:2: Financing eligible salaries and allowances of teachers and health workers	0.0	3.0	3.0	3.0	3.2	1.8	**14.0**
Sub-Component 3:3: Financing eligible non-salary recurrent costs in the health and education sectors	0.5	1.0	1.0	1.0	1.0	0.0	**4.5**
SUB-TOTAL for COMPONENT 3	**2.0**	**4.0**	**4.0**	**4.0**	**4.2**	**1.8**	**20.0**
Component 4: **Project management and coordination:** Includes EAFS consultants; workshops, seminars, training, travel, communications, translation of documents, operational expenses, bank charges etc.	1.7	1.8	1.8	1.8	1.9	**0.0**	**9.0**
SUB-TOTAL for COMPONENT 4	**1.7**	**1.8**	**1.8**	**1.8**	**1.9**	**0.0**	**9.0**
TOTAL	**24.0**	**30.0**	**30.0**	**30.0**	**28.2**	**1.8**	**144.0**

[20] The annual amounts of these transfer grants would have to be fully budgeted in FGSs Annual Approved Budget. For 2015, only US$3.0 million has been approved, hence a supplementary allocation would have to be approved by FGS before this component can be fully financed under the project.

[21] This component would be included in the approved annual budget of the FGS and transfers made to the appropriate sub-national authority.

Table 10: Breakdown of Total Project Costs and Financing for Each Entity

FEDERAL GOVERNMENT OF SOMALIA	INDICATIVE AMOUNTS						
	2015	**2016**	**2017**	**2018**	**2019**	**2020**	**TOTAL**
Component 1: Support to core government functions of MDAs in FGS	**16,000,000**	**18,000,000**	**18,000,000**	**16,000,000**	**13,000,000**	**-**	**81,000,000**
Sub-component 1.1: Financing eligible civil service salaries in the non-security sectors in FGS	13,000,000	12,000,000	10,000,000	8,000,000	6,000,000	-	49,000,000
Sub-component 1.2: Financing salaries and allowances for FGS staff under the CIM	2,000,000	4,000,000	5,000,000	4,000,000	2,000,000	-	17,000,000
Sub-component 1.3: Financing eligible non-salaries recurrent costs in the non-security sectors in FGS	1,000,000	2,000,000	3,000,000	4,000,000	5,000,000	-	15,000,000
Component 2.1: Inter-governmental fora on transfers and information exchange	**300,000**	**200,000**	**200,000**	**200,000**	**100,000**	**0**	**1,000,000**
Component 3: Support to recurrent costs in health & education sectors	**500,000**	**1,950,000**	**1,950,000**	**1,950,000**	**1,950,000**	**500,000**	**8,300,000**
Sub-component 3.1: Setting up basic accountability systems	300,000	-	-	-	-		300,000
Sub-component 3.2: Eligible salary & allowances of education & health workers	0	1,500,000	1,500,000	1,500,000	1,500,000	500,000	6,000,000
Sub-component 3.3: Non salary recurrent costs for education & health	200,000	450,000	450,000	450,000	450,000		2,000,000
Component 4: Project management & coordination	**820,000**	**1,470,000**	**1,470,000**	**1,470,000**	**1,590,000**		**6,450,000**
TOTAL	**17,620,000**	**21,620,000**	**21,620,000**	**19,620,000**	**16,640,000**	**500,000**	**96,750,000**
PUNTLAND		**INDICATIVE AMOUNTS**					
	2015	**2016**	**2017**	**2018**	**2019**	**2020**	**TOTAL**
Sub-component 2.1: Transfer to eligible federal member states, interim and emerging administrations for core government functions	**1,900,000**	**2,650,000**	**3,500,000**	**3,900,000**	**3,550,000**	**-**	**15,500,000**
CIM staff	1,100,000	2,100,000	3,200,000	3,200,000	2,100,000	-	**11,700,000**
System strengthening/access or eligibility criteria support	300,000	250,000	-	-	-	-	550,000
Non salary recurrent costs	300,000	300,000	300,000	400,000	450,000	-	1,750,000
Other support & contingencies	200,000	-	-	300,000	1,000,000	-	1,500,000
Component 3: Support to recurrent costs in health & education sectors	**1,200,000**	**1,200,000**	**1,100,000**	**1,100,000**	**1,250,000**	**500,000**	**6,350,000**
Sub-component 3.1: Setting up basic accountability systems	300,000	-	-	-	-	-	300,000
Sub-component 3.2: Eligible salary & allowances of education & health workers	700,000	950,000	850,000	850,000	1,000,000	500,000	4,850,000
Sub-component 3.3: Non salary recurrent costs for education & health	200,000	250,000	250,000	250,000	250,000	-	1,200,000
Component 4: Project management & coordination	**150,000**	**150,000**	**150,000**	**150,000**	**150,000**	**150,000**	**900,000**
TOTAL	**3,250,000**	**4,000,000**	**4,750,000**	**5,150,000**	**4,950,000**	**650,000**	**22,750,000**

INTERIM JUBBA ADMINISTRATION		INDICATIVE AMOUNTS					
	2015	**2016**	**2017**	**2018**	**2019**	**2020**	**TOTAL**
Sub-component 2.1: Transfer to eligible federal member states, interim and emerging administrations for core government functions	**1,400,000**	**2,400,000**	**1,900,000**	**2,200,000**	**2,650,000**	**-**	**10,550,000**
IJA salary payments for 18 civil servants supported by SFF	100,000	100,000	100,000	100,000	100,000	-	500,000
IJA competitively recruited staff	900,000	1,900,000	1,600,000	1,500,000	1,200,000	-	7,100,000
IJA system strengthening/access or eligibility criteria support	400,000	200,000	-	-	-	-	600,000
IJA non-salary recurrent costs	-	200,000	200,000	300,000	350,000	-	1,050,000
other support & contingencies	-	-	-	300,000	1,000,000	-	1,300,000
Component 3: Support to recurrent costs in health & Education sectors	**300,000**	**500,000**	**600,000**	**600,000**	**700,000**	**500,000**	**3,200,000**
Sub-component 3.1: Setting up basic accountability systems	200,000	-	-	-	-	-	200,000
Sub-component 3.2: Eligible salary & allowances of education & health workers	-	300,000	400,000	400,000	500,000	500,000	2,100,000
Sub-component 3.3: Non salary recurrent costs for education & health	100,000	200,000	200,000	200,000	200,000	-	900,000
Component 4: Project management & coordination	**80,000**	**80,000**	**80,000**	**80,000**	**80,000**	**80,000**	**480,000**
TOTAL	**1,780,000**	**2,980,000**	**2,580,000**	**2,880,000**	**3,430,000**	**580,000**	**14,230,000**

OTHER SUB-NATIONAL GOVERNMENTS	INDICATIVE AMOUNTS						
	2015	**2016**	**2017**	**2018**	**2019**	**2020**	**TOTAL**
Sub-component 2.1: Transfer to eligible federal member states, interim and emerging administrations for core government functions	**300,000**	**950,000**	**600,000**	**1,900,000**	**2,800,000**	**-**	**6,550,000**
CIM staff	-	350,000	300,000	850,000	1,000,000	-	2,500,000
System strengthening/access or eligibility criteria support	300,000	500,000	200,000	200,000	150,000	-	1,350,000
Non-salary recurrent costs	-	100,000	100,000	150,000	200,000	-	550,000
Other support & contingencies	-	-	-	700,000	1,450,000	-	2,150,000
Component 3: Support to recurrent costs in health & education sectors	**1,050,000**	**350,000**	**350,000**	**350,000**	**250,000**	**-**	**2,350,000**
Sub-component 3.1: Setting up basic accountability systems	700,000	-	-	-	-	-	700,000
Sub-component 3.2: Eligible salary & allowances of teachers & health workers	250,000	250,000	250,000	250,000	250,000	-	1,250,000
Sub-component 3.3: Non salary recurrent costs for health & education	100,000	100,000	100,000	100,000	-	-	400,000
Component 4: Project management & coordination	**-**	**100,000**	**100,000**	**100,000**	**100,000**	**100,000**	**500,000**
TOTAL	**1,350,000**	**1,400,000**	**1,050,000**	**2,350,000**	**3,150,000**	**100,000**	**9,400,000**

SOMALIA: Recurrent Cost and Reform Financing Project: Phase II

Annex 3: **Implementation Arrangements**

Project Institutional and Implementation Arrangements

1. Governance and organizational structure. The FGS will provide strategic direction with respect to policy and financing. To avoid an overly complex structure and to lower transaction costs, the project will use existing aid coordination architecture, including the SDRF. The proposed governance arrangements will consist of the project coordinating committee and the PFM reform coordinating unit, which would work closely with the EAFS team in the office of the Accountant General for project implementation. The governance arrangements include the following:

a. The **Project Steering Committee** will be chaired by the Minister of Finance of FGS or his/her deputy and will meet at least twice a year. The members would comprise Ministers of Finance or representatives from the participating eligible federal member states, interim and emerging administrations, and the Directors General from relevant ministries. Specific responsibilities include providing overall direction for the program, approving programs, budgets, and providing policy guidelines and directions.
b. A **Project Management Team** would be made up of the director general (DG) Ministry of Finance, the budget director, the accountant general, EAFS and CBS representatives, the project coordinator and consultants. This team will meet monthly and be responsible for providing technical guidance on the implementation of the project. The meetings shall be chaired by the DG of Finance. Additionally, the Public Financial Management Reform Coordinating Unit (PFMRCU) will be responsible for the overall coordination and day-to-day implementation of the project. Each state will engage a project manager that will be responsible for implementation in their entity.
c. An **External Assistance Fiduciary Section (EAFS)** has been established in the Accountant General's Department and supported under the PFM Strengthening Project. Plans are underway to establish similar Units in Puntland. The Project will seek opportunities for collaboration with the SSF in the IJA region, particularly in regard to payroll management and the establishment of the EAFS units. The EAFS units will be responsible for major implementation with support of external technical assistance. The EAFS Units will ensure harmonization, donor coordination, and reduced duplication, fragmentation and proliferation of donor-specific financial management units. Additional technical assistance will be engaged under the PFMCSP to support specific areas in financial management and procurement. The relevant FM, procurement and disbursement colleagues, as well as technical experts (particularly with respect to payroll engagement) will assess the implementing agencies. The EAFS will be responsible for fiduciary coordination of the Project, including salary payment arrangements. The organizational chart of the EAFS is in Figure B. Project monitoring, evaluation and reporting on progress and results will be carried out by the EAFS and will be expanded to include a unit for this function. This arrangement is expected to promote a high level of synergy and complementarities, eliminate unnecessary duplication and promote program ownership by government.
d. The **independent agent(s)** currently being engaged for the entire MPF will support third-party independent confirmation and verification of expenditures, including salaries and non-salary, recurrent cost expenditures, as well as capacity building for EAFS. Independent agent(s) will monitor, review and recommend for approval, withdrawal applications and all expenditures related to this Project, including non-salary operating costs. They will be responsible for the

review of personnel and payroll, expenditures review and other fiduciary compliance. Adequate fiduciary arrangements will be factored into the terms of reference of the technical assistance so as to ensure sustainability through knowledge-transfer to government staff, including suitable ways to measure the results of knowledge transfer.

e. Implementation arrangements for other interim and emerging states will be updated when the appropriate authorities come into existence and are included in the Project.

Financial Management and Disbursements

Country Issues

2. A key PFM finding of the 2006-2007 Joint Needs Assessment (JNA) of PFM systems in Puntland, Somaliland and South Central Regions[22] was that 'systems that manage public resources are weak'. Similarly, the April 2013 PFM self-assessment that focused mainly on central government PFM activities revealed serious capacity weaknesses similar to those identified by the JNA. However, in support of the Paris Declaration on Aid Effectiveness (2005), the Principles for Good International Engagement in Fragile States and Situations (2007), the Accra Agenda for Action (2008), and the Busan Partnership for Effective Development Co-operation (July 2012), there is a deliberate effort, as part of the New Deal 'FOCUS' and 'TRUST' principles, to utilize country systems. The underlying principle is *'country-ownership'* (anchored in the "strengthened PFM approach"), a common framework that has been widely agreed between the World Bank and development partners, and is in line with the World Bank's overall approach to strengthening its PFM work.

Project Financial Management System

3. An EAFS was established at the Federal Ministry of Finance [23] and has been operational for more than 1 year. With an increase in the number of externally financed projects, the FGS EAFS unit is being reorganized for greater effectiveness and responsiveness. In Puntland, plans are at an advanced stage to establish a similar unit, with a draft EAFS manual being prepared and reviewed by the Bank. In IJA, the project will work in close consultation with the SSF to support the civil servants payroll systems, and establish and build the capacity of IJA EAFS unit. The EAFS units will be charged with the responsibility of overseeing the financial management function for all the donor-funded projects implemented within Federal and States Government systems. In particular, the units will ensure the harmonization of their external assistance financial management function and donor co-ordination, and will work to reduce duplication, fragmentation and proliferation of donor-specific financial management units. The EAFS units will form part of the Project's financial management team, with responsibilities for day-to-day financial management of Project funds. The Project's financial management function will be carried out in line with the provisions of the respective EAFS manuals. The organizational structure of EAFS takes into consideration the key areas of authority, responsibility and appropriate lines of reporting. The basic functions of the EAFS will be planning, budgeting, and maintenance of internal control systems; as well as, accounting, reporting and liaising with external auditors on recipient-executed external assistance. The recommended organizational chart is depicted in Figure 4 (FGS and Puntland) and 5 (IJA) of this Annex. A team of consultants who will provide targeted technical assistance and on-the-job capacity- building support will support the EAFS units. The offices of the accountant general will need to identify an adequate office space to

[22] Jointly carried out by the Transitional Federal Government, the United Nations and the World Bank

[23] Office of the Accountant General

house the EAFS units and the team of consultants providing technical assistance to the EAFS. The EAFS offices will be equipped and furnished through the support of the Project.

Figure 4: FGS and Puntland EAFS Approval Hierarchy

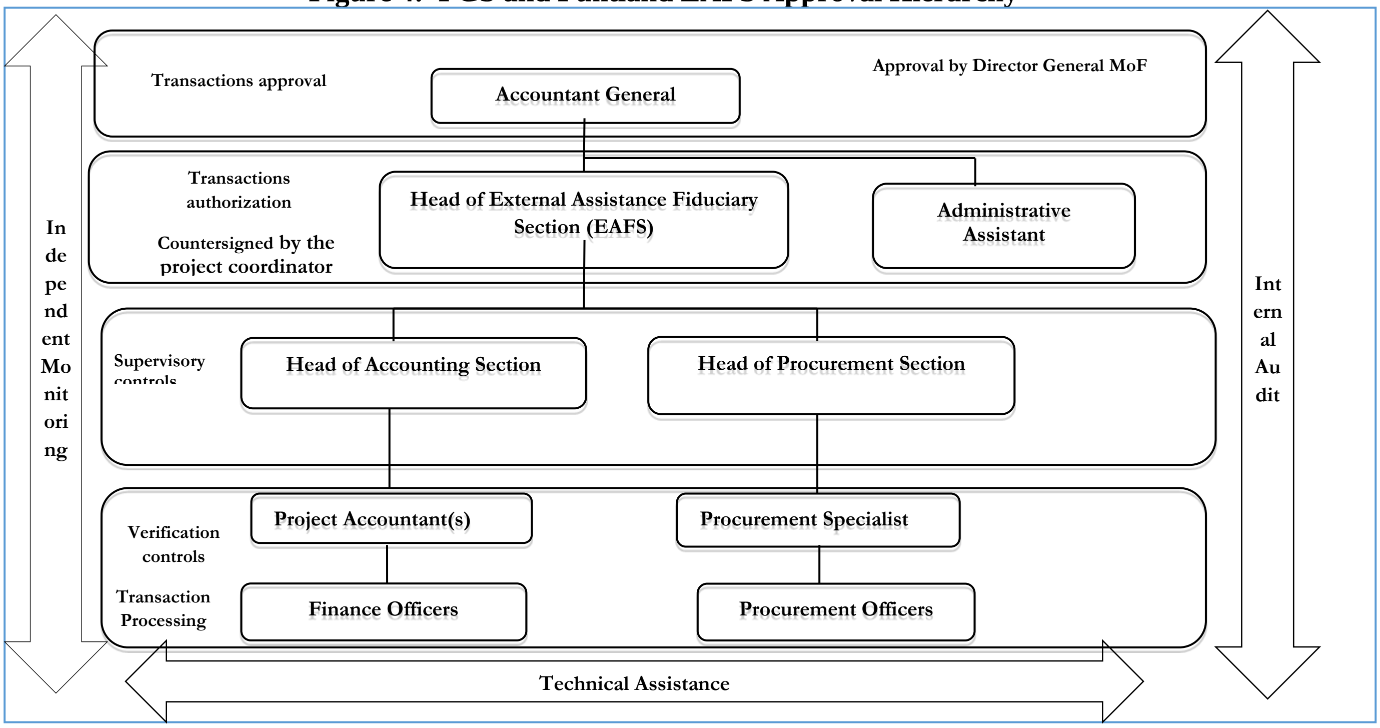
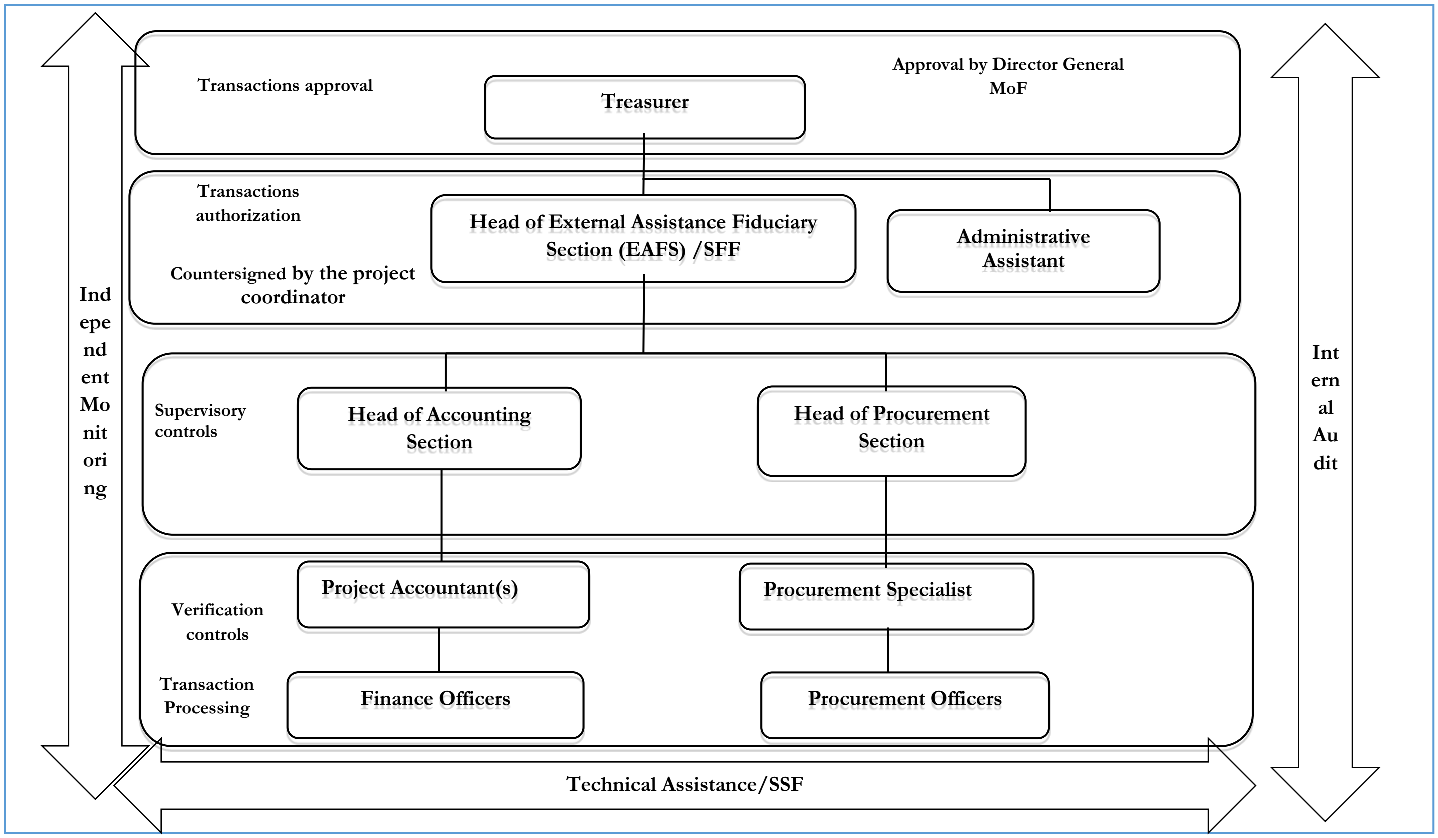


Figure 5: IJA EAFS Approval Hierarchy



Budgeting Arrangements

4. The FY 2015 annual budgets for the FGS, Puntland and IJA have been prepared, endorsed by the Councils of Ministers and appropriated by parliaments in the respective authorities. Although there has been evidence of fiscal transfers from the FGS to the States, inter-governmental fiscal relations between central and states governments is weak. As a result, the existing and emerging states' budget-estimates are not consolidated and included into the FGS annual budget estimates. The Project will seek to strengthen existing inter-governmental fiscal transfer arrangements. Under the Project, each of the EAFS units will prepare and submit through the FGS, Project annual work plans, and budget and detailed cash flow forecasts for necessary review and approval. The work plans, cash flow projections and budget estimates will include the figures for the year delineated into FGS and the participating states. The work plans and cash projections will reflect detailed specifications for Project activities to be undertaken, schedules (including procurement plans) and projected expenditures under Project activities. All annual work plans and cash flow forecasts will be sent to the TTL at least two months before the beginning of the fiscal year for review and approval. The Project's estimated annual disbursements for each of the Project components will be integrated and aligned into the FGS and state budget calendars ('on-budget) and will form part of the appropriated budget by FGS and the states. Budget utilization reports shall be prepared from the financial management systems as part of the internal governments' periodic reports, as will quarterly reports submitted to the World Bank.

Accounting Arrangements

5. FGS has developed a Somalia Financial Management Information System (SFMIS) - Bespoke. This includes a payroll module and is based on a comprehensive GFS and Classification of Functions of Government (COFOG), compliant with the Standard Chart of Accounts (SCoA). The use of the SFMIS has been strengthened through the FY 2015 Appropriation Act that requires all revenue and payment transactions be processed through the SFMIS and reconciled with the bank statement from the

Central Bank. The Somalia Stability Fund (SSF) has been supporting IJA to carry out PFM reforms. With support from SSF, IJA has developed GFS SCoA,[24] rolled out BISAN FMIS,[25] developed Ministry of Finance organizational structure, designed and implemented a system to disburse the SSF financing through TSA under the Ministry of Finance and prepared a reconciliation of outstanding salary arrears. With support from UNDP, Puntland has developed GFS compliant with SCoA, initiated rollout of the SCoA across all the MDA and developed and agreed formats to prepare the FY 2015 annual financial statement (AFS) using the IPSAS Cash Basis of Accounting. The development and rollout of FMIS for Puntland has been planned for under the Bank-supported PFM project. The Project's financial management function shall be migrated into FMIS once the Puntland FMIS is operational.

6. The Project's financial transactions will be captured, recorded, analysed, summarized and reported in line with the provisions of the International Public Sector Accounting Standards (IPSAS) Cash Basis of accounting. Appropriate records and documentation to track commitments and to safeguard assets will support these. To facilitate preparation of the relevant reports and annual financial statements, the project budgets and expenditures will be recorded and classified according to the approved SCoA at the FGS and state levels. The Project will be required to provide periodic and annual reports covering total Project expenditures; total expenditure on each of the Project's components/activities, and analysis of that total expenditure into various categories of goods, training, consultants and other procurement and disbursement categories. In addition, the FMIS payroll modules for FGS and IJA will be configured to provide Project-specific reports. The Project's financial management arrangements will be spelled out in the respective EAFS units manuals and will include all the relevant accounting procedures. The Project's reported financial transactions will cover all Project funds from the World Bank and any other contributions under the Project. Eligibility of expenditures will be based on the actual amount incurred and supported by appropriate documentation. Accounting records will be maintained in the United States of America Dollars (US$). The EAFS units, will ensure the following:

- All important project business and financial processes are adhered to;
- Adequate internal controls and procedures are in place;
- Accounting records and requisite supporting documents are maintained;
- Interim un-audited Financial Reports (IFRs) are prepared on a timely basis;
- Financial statements are prepared on a timely basis and in accordance with International Public Sector Accounting Standards (IPSAS *cash-basis*);
- External audit is completed on time and audit findings and recommendations/issues raised in the management letter are resolved judiciously.

Internal Control and Internal Auditing

7. The Project EAFS Manuals will be reviewed and updated to ensure they incorporate relevant emerging internal control procedures and acceptable control procedures for approval and payment processes. In addition, the Project will prepare a detailed Project Implementation Manual (PIM). The PIM will outline the key aspects of the Project operations, technical and financial management arrangements. The Project will institute controls and procedures to ensure goods and services are verified and certified before release of payments. The EAFS units will ensure that invoices and payment requests are consistent with signed contracts before processing and release of payments. They

[24] Plans are underway to review and align to SCoA to COFOG.

[25] Budget, expenditure, payroll and fixed assets module. A standalone Revenue Management System is being developed and will be integrated with the FMIS.

will also monitor and report on the utilization of Project funds, including the fiduciary standards and the reliability of the FM systems. A Project fixed assets register will be prepared, regularly updated, and physical verification of assets routinely carried out. The fixed assets register will reflect: details of suppliers; a description and location of goods; original costs; disposal of assets; assets reference (identification) numbers; serial or registration numbers; dates of purchase; assets additions; condition of assets; assets' useful life and residual value. Contracts Registers will also be maintained with respect to all contracts with consultants, contractors and suppliers. The EAFS units will prepare contract status reports quarterly as part of the IFRs. Control procedures over fixed assets and contracts management will be the responsibility of the implementing ministries.

8. An internal audit function once established will be mainstreamed into Project activities. The Project will liaise with the internal audit units to ensure that Project internal audit reviews are included in the annual work plans. The internal audit reports shall be prepared and shared with the Project operating teams and made available to the World Bank team during Project supervision. It is, however, important for the internal audit capacity to be strengthened and linked with other governments' and development partners' capacity-building interventions. In particular, an internal audit function will be required to carry out risk-based systems audits to strengthen the Project's internal control systems.

Financial Reporting Arrangements

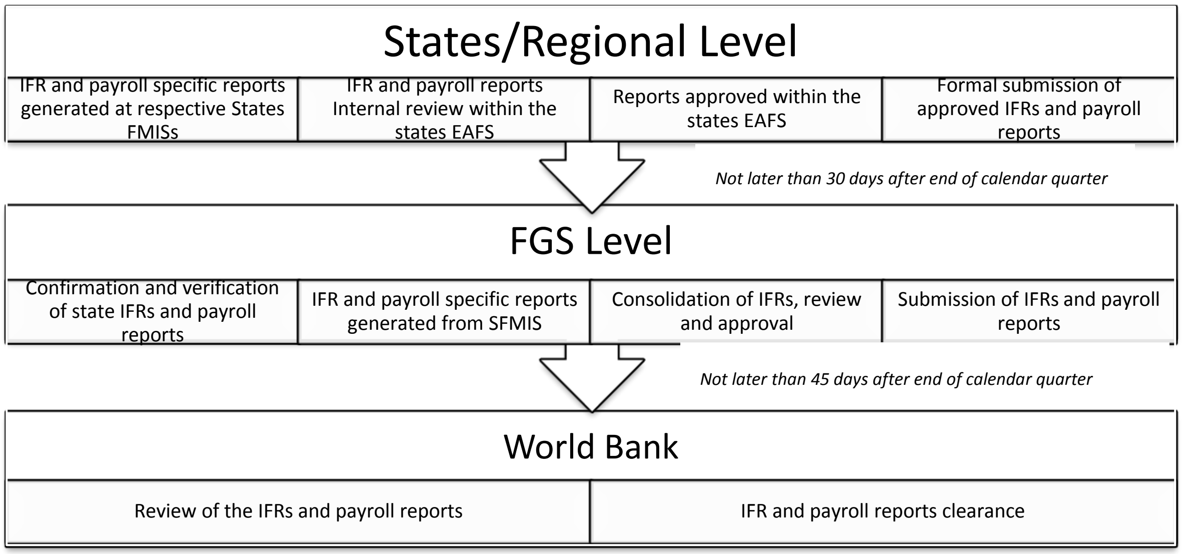
9. FGS annual financial statements for FY 2014 were prepared directly from the SFMIS.

10. In addition, RCRFP I and PFM projects' quarterly IFRs and IPSAS cash basis AFS are generated directly from the SFMIS. The system has been configured to accommodate existing and pipeline projects. Government-wide financial management reports in IJA are captured and reported through the BASAN FMIS. IJA has prepared 6 months of IPSAS cash basis compliant with AFS for the period of June to December 2014. In Puntland, government financial reports are prepared manually on hard-copied ledgers and in some cases summarized using Microsoft Excel sheets.

11. The states' EAFS Units will prepare and submit approved copies of IFR to FGS not later than 30 days after the end of the calendar quarter Interim Unaudited Financial Reports (IFRs). The FGS EAFS unit will prepare and submit approved consolidated IFRs not later than 45 days after the end of the quarter. The reports shall be consolidated and reported according to each of the Designated Accounts (DAs). *The IFRs shall report on all funds received under the Project as a whole, including any counterpart or government funds received under the Project.* The reports shall include a statement showing: period and cumulative inflows by sources and outflows by main expenditure classifications; beginning and ending cash balances and supporting schedules comparing actual and planned expenditures. All IFRs submitted by the states to FGS and by FGS to the Bank shall be duly approved. Expenditures shall be classified by component, sub-component and by categories. Semi-annual cash forecast statements should also be included. *The IFRs shall be prepared in the format and content as discussed and agreed between the government and the Bank*. The FGS and states FMIS shall be configured to facilitate timely and accurate generation of the IFRs, directly from the systems. In the interim period, pending the rollout of the Puntland FMIS, pre-designed Microsoft Excel worksheets, as discussed and agreed with the World Bank, will be used. *The FGS and states FMISs SCoA and FMIS shall be reviewed and aligned to facilitate bulk upload of detailed Project expenditures, according to the various dimensional analysis*. An adequate filing and archival system of all accounting and relevant supporting documents will be maintained at the EAFS units for review by the Bank's FM team during supervision (and for audit purposes). The IFR preparations and submission processes are summarized in figure 6 below.

12. The states' EAFS units will also prepare the Project's annual financial statements (AFS) and formally submit them to EAFS units at the FGS within 2 months after the end of the financial year. In parallel, the states EAFS units will also submit signed AFS to the respective states' offices of the auditor general in line with the state authorities' requirements. FGS will prepare consolidate AFS covering all the activities of the Project both at the states and FGS. Signed consolidated AFS for the Project shall be submitted to the FGS auditor general for external auditing not later than 3 months after the end of the financial year. The Statement will be prepared in accordance with cash basis IPSAS as shall be agreed between the Government and the Bank. The AFS will include adequate notes and disclosures consistent with the cash basis of financial reporting under the IPSAS.

Figure 6: Quarterly IFR Preparation and Submission Process



Auditing

13. Article 1 of Law 34 of 1972, the Somalia Law on the Magistrate of Accounts, creates the Office of the Auditor General. This law provides that the auditor general will be appointed by the President and is subordinate to the Presidency. Article 10 of Law 34 of 1972, the Law on the Magistrate of Accounts, require that no later than the 31st of May each year, reports on the annual accounts shall be transmitted to the Secretary of State for Finance. These provisions of the law, for all practical purposes, weaken the independence and effectiveness of the Office of the Auditor General to function as a Supreme Audit Institution (SAI). So far, KPMG as contractors under the UN-SIDP has provided support to the Auditor General's Office in Puntland and the Federal Government and has developed a Regularity Audit manual (Draft 12.01.2014) with the necessary working papers, templates and tools. A number of activities have been lined up for support of the FGS and Puntland Offices of the Auditor General (Supreme Audit Institutions – SAI). These include: Amendment and translation of the Audit Bills; development of strategy and action plans benchmarked with international best practices; [26] International Standards of Supreme Audit Institutions; development of Risk-Based Auditing (RBA) procedures manuals; supportive intra-regional/sub-regional peer learning events; as well as participatory diagnostic assessments. In IJA, an auditor general has been appointed. IJA authorities have requested SSF to assist in the establishment of the IJA Supreme Audit Institution (SAI), developing an audit Act and staffing and training the organization.

14. The Office of the Auditor General at the Federal level and in each of the states has the constitutional responsibility to carry out independent audit of all public entities. The FGS office of the auditor general will provide a consolidated project external audit report. In carrying out the external audit, the FGS office of the auditor general will work in close collaboration with the respective offices of the states' auditors general. In an effort to guarantee quality and timely audits, the project financial audit will be carried out with the support from technical assistance rendered by a qualified and certified auditor (or auditors) from a recognized professional auditing association. The Project will support the financing of the technical assistance and related expenses incurred by the offices of the auditor general

[26] AFROSAI-*E* SAI Institutional Capacity Building Framework (ICBF) and the INTOSAI SAI Performance Measurement Framework (SAI PMF)

in conducting the Project's external audit. The Project will ensure adequate budgetary provisions for the external audit costs, as they are provided under the aegis of the Project. The audited Project annual financial statements, together with any additional information required, will be submitted to the Bank not later than six months after the end of the fiscal year (or the closure of the project, as may be applicable). This audit will be in conformity with the Bank's audit requirements and in accordance with internationally recognized auditing standards. The auditor will express an opinion on the financial statements in compliance with ISA. In addition to the audited financial statements, the auditor will prepare a management letter with observations and recommendations for improvement in accounting, recording, systems and compliance with the financial covenants in the grant agreement. The external auditors will pay special attention to the risks of material misstatement of the financial statements due to fraud, in line with International Standards on Auditing (ISA) 240: "The auditor's responsibilities relating to fraud in an audit of financial statements".

Fraud and Corruption

15. A number of fiduciary risks that are likely to negatively impact the Project exist. These include: (i) the possibility of circumventing the internal control systems; (ii) colluding practices, such as bribes and illegal withdrawals; (iii) abuse of administrative positions; (iv) mis-procurement; (v) inadequate, and/or late submission of supporting documents; (vi) poor filing of records; (vii) unauthorized access to essential systems and information; (viii) lack of sufficiently detailed work plans and lack of fiscal discipline; (ix) unauthorized commitments and payments to suppliers; (x) bypassing budget and expenses control procedures; (xi) unsecured safekeeping and transportation of funds; (xii) unregulated banking and funds flow systems; (xiii) uncertainty over the banking arrangements supporting the Project; (xiv) potential exposure to money-laundering; and (xv) insecurity and political instability- among others.

Flow of Funds and Banking Arrangements

16. There is a Central Bank of Somalia Act 2011 and a Financial Institutions Law No. 130 of 22 April 2012 that provide for the licensing, regulation and supervision of the business of entities taking deposits from the public. The CBS has developed specifications for a National Payment System and a strategic plan to address its capacity challenges. Provisional licenses have been granted to the money transfer companies. 1.5 percent is deducted from all revenue deposited in CBS to fund its operations.[27] There is an on-going dialogue between IJA and CBS to establish CBS banking operations in IJA (Kismaiyo). Puntland had established banking operations with First Community Bank in Kenya. However, this banking corridor has faced uncertainties following the suspension and freeze of bank accounts of money-transfer companies in Kenya- most of which have been providing intermediary banking services to Puntland and, by extension, to Somalia.

17. The project will open two Designated Accounts (DAs) at the CBS, Mogadishu. Disbursements earmarked for the FGS will be disbursed through one of the DAs (DA1), while allocations for the states will be disbursed through the second (DA2). Disbursements for the FGS and the states will be maintained in separate bank accounts and will not be comingled. The project will open and operate a separate US$ Project Account (PA) in each of the states. Initial disbursement from the DA to the PAs will be based on ceiling as defined in the disbursement letter. Subsequent replenishments of the PAs will be disbursed SOE basis. All the expenditures incurred through the PAs and DAs, as well as those submitted to the World Bank for direct payments will be justified, supported, and eligible as defined in the PAD and the Grant Agreement(s). All project withdrawal applications to the Bank will be made in

[27] As at end June 2013, CBS earned US$795,993.92 from such deductions.

US$ and will be submitted online through the client connection. Designated staff within FGS EAFS will have requisite access to the client connection while those in the eligible regional states, interim and emerging administrations will have access to input and submit withdrawal applications to the signatories". Replenishment and reimbursement withdrawal applications will be accompanied by statements of expenditures (SOE) in accordance with the procedures established in the disbursement Letter and the Bank's disbursement guidelines. Detailed disbursement arrangements will be documented in the disbursement letter. The Project will liaise with the CBS to discuss and agree on reasonable and agreeable charges and/or commissions on grant transactions. The EAFS units will institute adequate controls in the management of the DAs, as well as the Project Accounts. The signatories to the DAs (treasury cheques/payment instructions/electronic funds transfer) and withdrawal applications will include at least two bank account signatories' categories (either from each panel must sign):

Designated Account and States Bank Project Accounts Signatories:

- Panel A: Director General of MOF (with Director of Administration as alternate)
- Panel B: Accountant General (with Deputy Accountant General as alternate)

Puntland Project Account

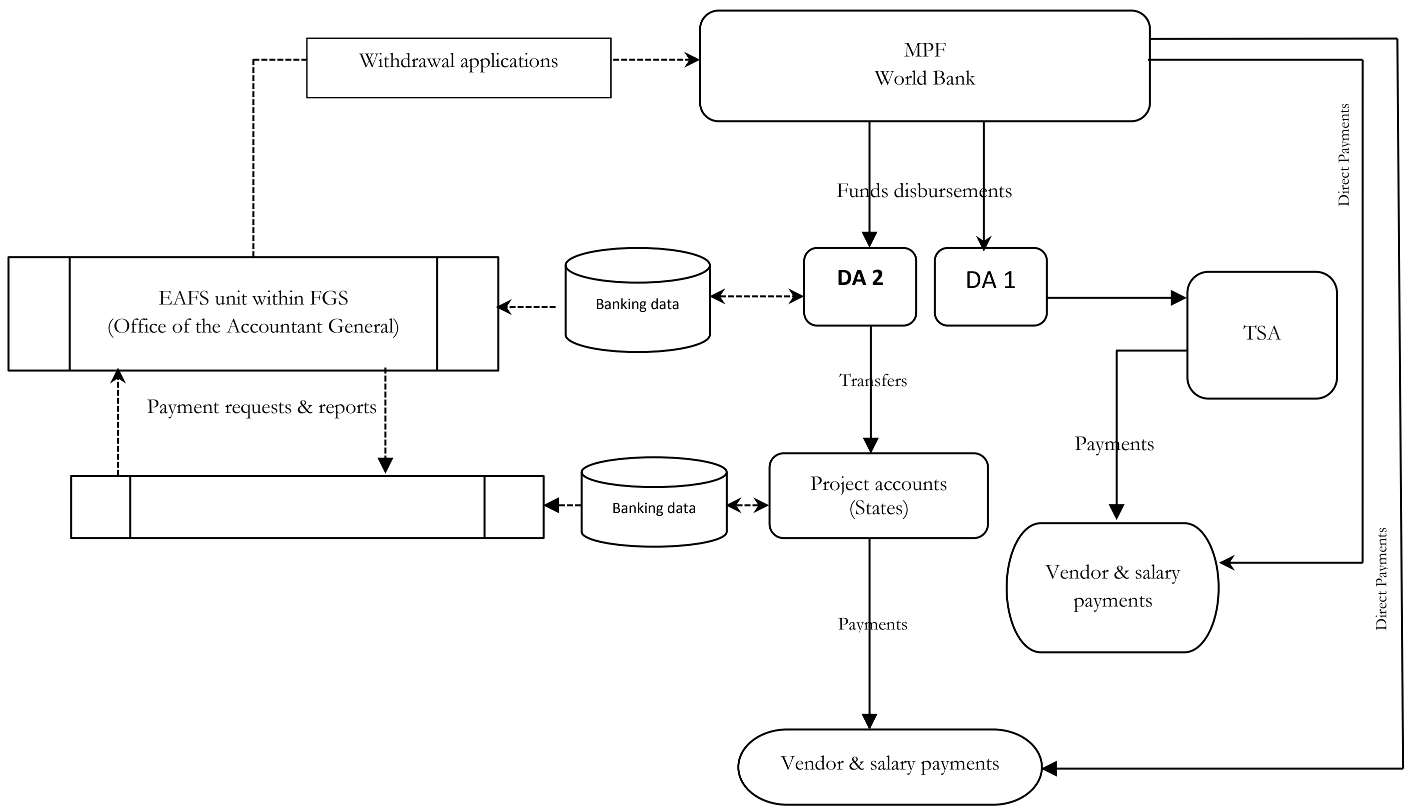
- Panel A: Director General of Expenditure (with Director General Inland Revenue as alternate)
- Panel B: Accountant General (with Deputy Accountant General as alternate)

IJA Project Account

- Panel Permanent Secretary (with Director of Administration as alternate)
- Panel B: Treasurer (with Accountant as an alternative)

18. The ceiling of the DA will be based on the cash-flow projections, as will be discussed and agreed between the Bank and the government. In the cases where certain expenditures are not financed 100 percent from Bank proceeds, the government will ensure that complementary financing is made available upfront prior to expenditure commitments. The Bank will only finance the agreed amount or applicable proportion of the overall approved expenditure categories. The government will make arrangements to ensure salary payments are expedited in a timely and practicable manner with requests for reimbursements submitted to an independent reviewer for verification and clearance. Subsequent withdrawal applications will be based on SOE reviewed and cleared by the Reviewer. All ineligible expenditures based on review and any additional due diligence will be deducted from subsequent withdrawal applications and the Project will be required to reimburse the applicable ineligible amounts. The funds flow processes for FGS and states are outlined in Figure 7 below.

Figure 7: Funds Flow process



19. Each of the EAFS units ensure:

i) A DA in US$ for the Project is opened in a financial institution acceptable to the Bank[28] and managed according to the provisions of the PAD and the grant agreement.
ii) Project component funds are transferred into the DA against approved withdrawal applications.
iii) Subsequent withdrawals are supported by SOE and the requisite supporting documentation.
iv) Disbursement arrangements, as documented in the disbursement letter, are adhered to.
v) Once the vendor registration data base and payment systems are established, salary payments and third party payments are processed directly into the vendors' and employees' accounts.

[28] On terms and conditions in the World Bank Disbursement Guidelines for Projects (May 1, 2006:11).

Table 11: Financial Management Action Plan:

	Action	FGS	Puntland	IJA
1	Set up and staffing/reorganization of the EAFS/equivalent units	30 June 2015	30 June 2015	30 June 2015
2	Develop/update EAFS manual	30 June 2015	30 June 2015	30 June 2015
3	Project implementation manual	25 June 2015	25 June 2015	25 June 2015
4	Migration of the existing payroll lists into the respective FMIS	25 June 2015	31 December 2015	25 June 2015
5	Configuration of the FMIS payroll module to accommodate the CIM/newly recruited staff.	25 June 2015	31 December 2015	25 June 2015
6	Review and alignment of existing SCoA to accommodate RCRFP specific requirements (FGS and COFOG)	30 June 2015	30 June 2015	30 June 2015
7	Configuration of the FMIS and payroll modules to generate required IFR and payroll specific reports	30 June 2015	31 December 2015	30 June 2015
8	Annual Financial Statements (AFS) content and formats	30 June 2015	30 June 2015	30 June 2015
9	Procedure and modalities of co-financing expenditures (salaries) that are not financed 100% by the Bank.	25 June 2015	25 June 2015	25 June 2015
10	External audit arrangements and ToR	25 June 2015	25 June 2015	25 June 2015
11	Open DAs and states project accounts	18 June 2015	18 June 2015	18 June 2015
12	Independent review arrangement	30 June 2015	30 June 2015	30 June 2015

Procurement

20. The FGS public procurement legal framework and institutions are not yet in place. The Country has neither the institutional capacity nor legislative framework to handle robust public procurement. The private sector and civil society have limited capacity or functionality (due to a total lack of regulatory law and business norms). A new public procurement, concessions & disposal bill has been approved by the Council of Ministers and is now in the Somalia National Parliament for discussion. If enacted, the new Act conceptualizes a decentralized system of procurement. The Act further provides for an independent oversight body that will foster the regulatory and the policy framework of public procurement in the country.

21. Procurement for the proposed Project will be carried out in accordance with the latest revision of the World Bank's "Guidelines: Procurement of Goods, Works, and Non-Consulting Services under IBRD Loans and IDA Credits & Grants by the World Bank Borrowers," (revised July, 2014); and "Guidelines: Selection and Employment of Consultants under IBRD Loans and IDA Credits & Grants by the World Bank Borrowers" (revised July 2014) provisions that facilitate working with the emergency and fragile situations in Bank-financed projects and Recipient–Executed Trust Funds. "Guidelines on Preventing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants, (the Anti-Corruption Guidelines)" (revised in January 2011), and the provisions stipulated in the Legal Agreement will be applied. Given that Somalia is in a Fragile and Conflict Affected Situation (FCS), Procurement under the Projects will be processed under special procurement arrangements referred to in paragraph 20 of OP 11.00.

22. Project procurement implementation arrangement and risk identification: (a) In the FGS the procurement of the proposed Project will be carried out by the EAFS unit in the MOF. (b) All procurements under the Project will be undertaken centrally by the EAFS unit under the accountant general's office in the Ministry of Finance. The EAFS unit is fully functional and supported by a

procurement specialist. Additional procurement expertise will be provided by the TA procurement specialist contracted by government after an intense competitive recruitment process and funded by the African Development Bank. The placement of the TA procurement specialist will mitigate against inherent procurement risks caused by capacity limitations to undertake proper and efficient project procurement. It is expected that the TA procurement specialist will ensure that procurement capacity is created within the Ministry of Finance. At least two government procurement officers will be seconded to the EAFS unit for the necessary mentoring and transfer of skills to be achieved by the procurement specialist. It is hoped that these officers will be absorbed into the national civil service to constitute a procurement unit for the MOF.

23. In Puntland, under the MOF, a similar EAFS will be established to provide procurement and FM support to all donor-funded projects. Procurement for the Project will be handled by EAFS. A procurement officer will be hired, with the necessary skills and experience, under the supervision of the EAFS in Puntland. His/her project procurement skills will be enhanced by guidance received from the TA procurement specialist in Mogadishu.

24. In Jubbaland, SFF will in the interim provide procurement support. After the EAFS is set up in Jubbaland, procurement responsibility will be gradually transferred to IJA. A procurement officer will be hired in year two of Project implementation, with the necessary skills and experience to be based in the region. His/her project procurement skills will be enhanced by guidance received from the TA Procurement Specialist in FGS.

25. As a result of the overall operational challenge and weak institutional capacity, the Project procurement risk is rated high. The major challenges related to the overall procurement environment and institutional capacity aspects and possible risk mitigation measures have been identified in table 3 below.

26. **Specific procurements under the Project**: Procurement under the Project includes: a number of consultancy services assignments (both firms and individual consultants); highly specialized ICT equipment; acquisition of bandwidth, etc., smaller goods and equipment and office supplies. These are elaborated in the procurement plan.

27**.** **Procurement and selection methods:** The procurement of goods and non-consulting services, where applicable, will utilize methods such as International Competitive Bidding (ICB), NCB, LIB, procurement from UN agencies, shopping, and direct contracting. Procurement from UN Agencies-such as UNOPS will be used for procurement of vehicles. Selection of consultants will follow QCBS, QBS, Selection based on consultants' qualifications (CQS), LCS, FBS, selection of individual consultants, and SSS.

28**.** **Workshops, conference attendance and study tours:** These will be carried out on the basis of approved annual work plans that would identify the general framework of training or similar activities, including the nature of training/study-tours/workshops, the number of participants, and estimated cost.

29. **Operating costs, excluding salaries, bonuses, and fees** for government civil servants, would be incurred using procedures acceptable to the Bank and described in the operation manual.

30. **Procurement plan.** The borrower has developed a procurement plan which has been reviewed by the Bank and is part of the PAD indicating procurements to be carried out in the first year of the project. The Procurement Plan will include all the contracts to be financed by the Project. The plan will be updated at least yearly over the lifetime of the Project. Any revision of the Procurement Plan will be subject to prior review by the Bank.

31. **Threshold for each method of procurement/selection and prior review**: Below are the recommended methods of procurement/selection and the prior review threshold requirements. Guidance for the Bank's prior review requirements is found in Appendix 1 to the guidelines for procurement and Appendix 1 to guidelines for selection and employment of the consultants. All terms of reference (ToRs), regardless of the contract amount, will be subject to the Bank's prior review.

Table 12: Action Plan, Procurement Risks and Mitigation Measures

No	Issue	Risk mitigation action plan	Responsibility and time frame to implement the actions
1	Lack of public procurement legal and institutional framework (including procurement regulations, procurement manual etc.) in all the areas	The manual developed by EAFS in MOF will guide the procurement in FRS. The Bank will review the updated Procurement Manual for use in the project. Deviations in these Manuals in procedures necessary to meet the requirements of the World Bank would be stipulated in the Project Operation Manual (POM).	EAFS/Immediately
2	Experience and skills limitations within the EAFS unit in Mogadishu, Garowe and Jubbaland.	In FGS, the EAFS unit will be supported by a TA procurement specialist and two (02) procurement officers locally recruited. In addition to processing the project procurement, the TA consultant will train the staff of EAFS to enable them to gradually assume the procurement activities of the Project; In Puntland and Garowe a qualified and experienced procurement officer will be hired.	MoF/ADB/June 2015
3	Lack of procurement regulation, oversight and monitoring arrangements for the project procurement	The EAFS unit will have a management structure to supervise and monitor and approve the implementation of the planned procurement activities and will work with EAFS for procurement monitoring and reporting.	EAFS/immediately
4	Absence of defined procurement complaints' handling mechanism	As the procurement law is not yet in place, any procurement complaints by dissatisfied bidders or stakeholders may be lodged with the accounting officer through the Head of the EAFS; and the coordinator has to respond to complaints within a reasonable time.	EAFS/immediately after receipt of the complaint
5	Because of security challenges and weak public sector functionality, the private sector participation and efficiency would be limited, affecting the	All bidding opportunities will be advertised on the available website and posted on a widely circulated national gazette. If the contract is ICB or if the assignment includes international firms, it has to be advertised on UNDB online in addition to the local posting. Private Sector orientation and outreach seminars will be conducted on Project opportunities.	EAFS/ regularly

	supply market functionality		

Table 13: Procurement Methods and Thresholds for Goods, Works and Non-Consulting Services

	Procurement Method	**Threshold(US$)**	**Comment**
1	ICB (Works)	5,000,000	Equivalent or More
2	ICB (Goods and non-consulting services)	500,000	Equivalent or More
3	NCB (Works)	5,000,000	Less than
4	NCB (Goods and non-consulting services)	500,000	Less than
5	Shopping (Works)	300,000	Equivalent or less
6	Shopping (Goods and non-consulting services)	100,000	Equivalent or less
7	Direct Contracting	Any value	
8	UN Agencies	Any value	

Table 14: Prior Review Thresholds for Goods and Non-Consulting Services

	Procurement Method	**Prior Review Threshold(US$)**	**Comment**
1	ICB (Goods, works and non-consulting services)	All contracts	
2	NCB (Goods, and non-consulting Services)	500,000	Equivalent or more (The first NCB under each category will be under prior review)
3	NCB (Works)	5,000,000	Equivalent or More (The first NCB will be under prior review)
4	Direct Contracting (Goods, works and non-consulting services)	All contracts	
5	UN Agencies	All contracts	
6	Shopping (Goods and Works and non-consultancy services)	None (See comment)	The First shopping under each category will be under prior review.

Table 15: Selection Methods and Thresholds for Consultants

	Selection Method	**Threshold(US$)**	**Comment**
1	QCBS, QBS, FBS and LCS	Any value	Selection method shall depend on nature and complexity of assignment.
2	CQS	300,000	Equivalent or less generally, however, may be permitted for higher value in appropriate cases as identified in Procurement Plan
3	Individual Consultant	Any value	
4	SSS (for individual/ firm)	Any value	

Table 16. Prior Review Threshold for Consultants

	Selection Method	**Threshold(US$)**	**Comment**
1	Competitive Methods (Firms)	200,000	Equivalent or More
2	Individual Consultant Selection	200,000	Equivalent or more
3	Single Source Selection (Firms/Individuals)	Any value	Equivalent or more

32. **Short list comprised entirely of national consultants:** Short lists of consultants for engineering and contract supervision assignment estimated to cost equal to, or less than, US$200,000 equivalent, and for all other consultancy assignments estimated to cost equal to, or less than, US$100,000 equivalent per contract, may consist entirely of national consultants in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines.

33. **Frequency of Procurement Supervision:** In addition to the Prior review supervision to be carried out by the Bank, annual post-procurement reviews of a sample of about 20 percent of all contracts finalized by the Project will be conducted.

Table 17: Draft Simplified Procurement Plan for 2015

	Contract description	Estimated cost (US$) 000's	Procurement method	Review by World Bank (prior/post)	Expected bid/proposal submission date	Expected contract signature	Expected completion date
	Component Two						
	Consultancies						
	Sub Component 2.1 Transfers to Interim and Emerging States						
2.1	TA- Strengthening/access on eligibility criteria for Puntland	550	ICS	Prior/post	July 2015	July 2015	July 2017
2.2	TA- Strengthening/access on eligibility criteria for- IJA	400	QCBS	Prior	July 2015	July 2015	July 2017
2.3	TA- Strengthening/access on eligibility criteria for Sub National Authorities	300	ICS	Prior/post	July 2015	July 2015	July 2020
2.4	TA - System Strengthening and establishment of Basic Accountability Systems	200	ICS	Prior/post	Aug 2015	Sept 2015	Sept 2015
	Sub Component 2.2 Inter-governmental Fora on Transfers & Information Exchange						
2.5	TA to FGS to support Interim and Emerging States in Inter-governmental Relations	100	ICS	Post	Aug 2015	Sept 2015	Sept 2015
	Component Three						
	Consultancies						
3.1	TA-support the setting up of accountability systems - FGS	300	ICS	Prior/post	July 2015	July 2015	Oct 2015
3.2	TA-support the setting up of accountability systems - Puntland	300	ICS	Prior/post	July 2015	July 2015	Oct 2016
3.3	TA-support the setting up of accountability systems - IJA	200	ICS	Prior/post	July 2015	July 2015	Oct 2017
3.4	TA-support the setting up of accountability systems - Others	700	QCBS	Prior	July 2015	July 2015	Oct 2020
	Component 4 Project Management – FGS						
	Project Management & Administration						
							Consultancies
4.1	PFM Deputy Coordinator	60	ICS	Post	July 2015	Aug 2015	Aug 2017
4.2	Head EAFS Consultant	58.8	ICS	Post	July 2015	Aug 2015	Aug 2017
4.3	Section Lead/Accounts	48.0	ICS	Post	July 2015	Aug 2015	Aug 2017
4.4	Consultants Accounts Section (3)	72.0	ICS	Post	July 2015	Aug 2015	Aug 2017
4.5	Senior Administrative Assistant	35.5	ICS	Post	July 2015	Aug 2015	Aug 2017
4.6.1	Impact Evaluation – Control Mechanism for Non-Salary Recurrent Expenses	28	ICS	Post	Sep 2015	Oct 2015	Oct 2015
4.6.2	Impact Evaluation - Linkages of pay to Performance in Health and Education Sectors	28	ICS	Post	Sep 2015	Oct 2015	Oct 2015
4.7	TA Assistance to Central Bank	60	ICS	Post	Sep 2015	Oct 2015	Oct 2015

	Support to other Sectors						
4.8	Individual Consultants	288.8	ICS	Prior/post	July 2015	Aug 2015	Aug 2017
4.9	External Audit Services	100.0	SSS	Prior	N/A	N/A	N/A
	Goods - FGS						
4.10	Purchase of Vehicle for FGS, Puntland IJA and new sub national	150	NCB	Post	July 2015	Aug 2015	Aug 2019
4.11	Purchase of Office Equipment and Computers for EAFS set up	150	NCB	Post	July 2015	Aug 2015	Aug 2019
	Component 4 Project Management and coordination - Puntland						
4.12	Head EAFS Consultant	58.8	ICS	Post	July 2015	Aug 2015	Aug 2017
4.13	Section lead - accounts	48.0	ICS	Post	July 2015	Aug 2015	Aug 2017
4.14	Consultants accounts section	24.0	ICS	Post	July 2015	Aug 2015	Aug 2017
4.15	Senior administrative assistant	40.0	ICS	Post	July 2015	Aug 2015	Aug 2017
	Component 4 Project Management and coordination – IJA						
4.16	Head EAFS consultant	58.8	ICS	Post	July 2015	Aug 2015	Aug 2017
4.17	Section lead - accounts	48.0	ICS	Post	July 2015	Aug 2015	Aug 2017
4.18	Consultants accounts section	24.0	ICS	Post	July 2015	Aug 2015	Aug 2017
4.19	Senior administrative assistant	40.0	ICS	Post	July 2015	Aug 2015	Aug 2017

Note:

1. The first contract of NCB and shopping will be subject to prior review.
2. For ICS where “Prior/Post” review is indicated, if the amount of single contract is USD 200,000 and above, that would be subject to prior review and if it is less than USD 200,000 will be subject to post review.

SOMALIA: Recurrent Cost and Reform Financing Project: Phase II

Annex 4: **Systematic Operations Risk-rating Tool (SORT)**

The assessment of risks takes into account both the likelihood of the risk materializing, as well as the severity of its impact on the achievement of the intended results. SORT focuses on identifying, assessing, and managing risks throughout an operation.

Risk Categories	**Rating (H, S, M or L)**
1. Political and governance	**Political and governance**: The Risks are **Substantial.** Changes in political leadership/appointees could undermine government ownership of the project and the initial gains made under the RCRFP Phase I Project. Political competition for Project resources is also substantial. Project staff will face difficulties in reaching agreements between key government stakeholders in the FGS, Puntland and the IJA on the overall division of resources and the implementation arrangements for the Project. Given the high levels of political and clan-based competition within government, procurement and, especially, the selection of consultants, there is the potential for divisiveness and unproductive competition within government, rather than the collaboration that is essential for systemic reform and the achievement of project/program results and outcomes. The task team will engage with multiple levels of leadership in the FGS, Puntland and the IJA, to ensure wide institutional ownership, thus mitigating risks posed by a turnover of politically appointed leaders. The task team and government counterparts also will engage in transparent dialogue with stakeholders in FGS, Puntland and the IJA on the allocation of Project resources. Strategic objectives will be clearly defined in order to resist pressures and resentment that the available funding is spread too thinly to meet political requirements; such pressures can endanger the adequacy of resources to fund the salaries and other recurrent costs of eligible civil servants. The Ministry of Finance in the FGS will anchor the project and its associated reforms and capacity- building efforts, helping to mitigate this risk at Ministerial levels in all three jurisdictions of the Project, providing the strategic alignment of the Project with the directives of the Oversight and Technical Steering Committees.
2. Macroeconomic	**Macroeconomic:** External and domestic economic risks can derail implementation and achievement of results and thus the risk rating is **High.** There is a lack of fiscal space for reforms because of the high security costs of attracting suitably qualified and experienced professionals to work in Somalia. Economic institutions are weak and macroeconomic policies are at high risk of becoming unsustainable and vulnerable to external shocks. Large annual fiscal deficits in the past two years (2013 and 2014) of 21 percent and 13 percent of total aggregate budgeted expenditures is a demonstration of this condition. The FGS has taken steps to address these imbalances, but these are still incomplete and lack credibility because of the government's weak track record. For example, key policies and required legislation (e.g. the Telecommunications Act) are yet to be passed to enhance revenue collection. Over the medium to long term, the project will strengthen

Risk Categories	Rating (H, S, M or L)
	civil servant salaries, and non-salary recurrent cost payment systems in FGS, Puntland and IJA—leading to greater efficiencies and effectiveness in government operations. This is likely to provide more fiscal space and better strategic use of scarce resources. Openness in budget information will also enable the private sector to plan better for supplying goods and services for the service delivery priorities of the government.
3. Sector strategies and policies	**Sector Strategies and policies.** The risks associated with the strategies and policies of the sectors relevant to the Project are rated as **Substantial.** Insufficient development of partner-cooperation is a risk. Potential fragmentation of the development of partner-support is a risk. Although Project preparation involved a highly consultative process with donor partners, it will be necessary to maintain this dialogue and collaboration throughout Project implementation, utilizing systematic sharing of Project information and including donor- partner staff in the supervision and implementation of support missions. The lack of coordination between Bank projects is also a moderate risk**.** Bank projects that target core government functions (capacity, PFM, payment of eligible non-military civil servant salaries and other non-salary recurrent costs) may not be coordinated sufficiently to deliver the desired results and outcomes in the most effective and efficient manner. Under this **Project,** the task-team will take a number of actions to mitigate these risks. First, it is actively involved with the PSG-5 working group. This group unites development partners and government representatives working on PFM (including civil service salary payment reform), and will thus help to ensure coordination and communication. Second, within the Governance Global Practice (GGP), the task teams of the related projects will maintain regular communication to ensure coordination. Also, the task-team will ensure strong collaboration with other GPs that contribute to project design and implementation; such as: Macroeconomic and Fiscal Management; Health, Nutrition & Population; Education GPs; and, the Fragility, Conflict & Violence CCSA. The MPF Secretariat will provide additional support for fund-level coordination of Bank activities.
4. Technical design of project or program	The risks related to the technical design of the project are **Substantial.** There are three main risks and these relate to: (a) Scope of project activities**.** Overall, the RCRFP reform agenda is ambitious, with multiple components cutting across key institutions and regional governments. Somalia's administrative and sectoral institutions will have limited ability to absorb resources and human capital at a rapid pace, or adapt to overly ambitious reform agendas. Moreover, the interconnectedness of the various RCRFP reform activities will need to be properly prioritized and sequenced to avoid delayed or sub-standard outputs, which will require intra-governmental coordination; (b) Weak PFM Systems**.** The RCRFP Phase 1 Project recognized that systems that manage public resources are very weak. Overall, the fiduciary environment has substantial weaknesses and the principles of transparency, accountability and participation are not being implemented. The PFM legal framework is outdated. Passage of the 2014 budget was substantially delayed by five months, and if this is repeated in 2015, it will delay Project implementation, since RCRFP Phase II will be "on-budget." Project financial reports

Risk Categories	Rating (H, S, M or L)
	will be produced from the SFMIS but delays can be expected. Commercial banking is still at the take-off stage and this leads to cash handling with all of the inherent risks of a leakage of funds. Project officials have been trained on use of the External Assistance Fiduciary Manual and they adhere to the procedures and manuals. An internal audit function is yet to be established. A qualified accountant general and auditor general were recently recruited. Annual financial statements and audit reports are up to date but Parliament is yet to consider the 2012 and 2013 audit reports to assess the extent of follow-up required on audit findings; and (c) Insufficient project funding: Insufficient funding to MPF to cover full Project costs could prevent implementation of all Project components. For each of these risks, the Project will institute mitigation actions. As regards the scope of the Project, reforms will be introduced gradually to ensure government ownership and incremental capacity-building tailored to the context. Implementation teams, led by senior Government officials supported by SMEs and technical assistance with skills-transfer mandates and appropriate change-management techniques, will mitigate the complexity of risks. Close monitoring of work plans by the project steering committee and management team will be critical. However, expectations should be managed, because financial resources and legal agreements, though necessary, are not sufficient. An environment with strong political leadership that provides for citizen participation to demand accountability is critical in achieving shared prosperity. There is also a deliberate effort to use and strengthen the use of country systems through technical assistance (SMEs) for skills-transfer. A key control is to shift from cash payment to ministry officials to direct payment to end-beneficiaries who would have been screened and captured in a vendor database. Also, payments instructions from the accountant general's department can only be authorized against a unique donor fund-source and Project component/sub-component and line item in the chart of accounts- for which there must be an approved budget and allocation. The payment instruction is bar-coded as an additional system control such that the CBS bank can only pay the amount stated in the instruction with a system-generated number to the named vendor. Finally, Project budgets are established based on donor commitments to the MPF. Project budgets are also based on CMU projections of the funds that will be available in the MPF, as well as on financial planning.
5. Institutional capacity for implementation and sustainability	Risks related to the capacity of the FGS to implement activities, taking into account the institutional capacity of the implementing agencies, implementation arrangements (including PIUs), and monitoring and evaluation arrangements is rated as **Substantial.** The client lacks familiarity with World Bank procedures and this may lead to delays in implementation, and capacity constraints within Ministries are high. Targeted Government institutions are staffed with unskilled, aged or absentee employees. Therefore, the Project may struggle to achieve the critical mass of capacity necessary to strengthen institutional capacity and implement reform. To overcome these risks, the Project will use and strengthen the country PFM and salary payment systems through EAFS arrangements. The World Bank will provide expanded

Risk Categories	Rating (H, S, M or L)
	support to the client through an implementation support team. Moreover, the team will hold regular dialogue with the client to explain procedures and provide support. Project design focuses heavily on training and technical assistance in key areas (e.g., Monitoring and Evaluation of results and outcomes; Project implementation planning and management; team and operational leadership; financial management & procurement) in the early stages of Project implementation. Also, the PFM and RCRFP education and training programs will produce a cohort of suitably qualified PFM and project planning and implementation practitioners. Finally, considering the need for flexibility, speed, and effectiveness, a list of "pre-selected" consulting firms and/or individuals is considered an appropriate method for supporting the Government at various steps of Project execution. Sole sourcing of consulting firms or individual consultants already working in similar areas, who have a proven track record for the provision of technical assistance, will also be considered.
6. Fiduciary	The risks are **High** that Project funds will not be used with integrity to achieve value for money. There are many reasons for this, but three stand out. First, there is limited financial management capacity. There is a lack of key financial management competencies, weak internal controls and oversight, rudimentary accounting and reporting systems, over-reliance on external, technical assistance, nonexistent banking arrangements, and inadequate internal and external audit arrangements. Second, there is a lack of public procurement guidelines and regulations, as well as a lack of experience and skills, which could slow implementation and create opportunities for corruption and fraud. Third, given the absence of a robust public financial legal framework and rudimentary banking systems, the risks of fraud and corruption are high. Other internal control weaknesses that may expose the Project to fraud and corruption include: (a) late submission of required supporting documents; (b) poor filing, and absence of minimum standards in the maintenance of Project accounting records; (c) noncompliance with approve Project work plans and/or budget discipline; (d) unauthorized commitment to suppliers; (e) bypassing agreed internal control oversight arrangements, particularly in expenditure management expenses; (f) high risks in cash handling inherent in the existing cash-driven dollarized economy; and, (h) denial of access to information and or limiting the scope of agreed external monitoring arrangements. To overcome these risks, the project will take mitigation actions as follow: Education and training components in the PFM and RCRFP, will, over time, deliver a cohort of suitably qualified PFM and payments professionals. The Capacity Injection project will also provide institutional support by developing appropriate HR policies and organizational development of key MDA. A major role of SMEs will be to mentor and transfer skills through coaching to ensure the long-term sustainability of the planned reforms. The use of country systems will be more developmental. The auditor general would have responsibility for carrying out the audit of the Project. However, because of current capacity constraints, an external audit firm acceptable to the Bank will be selected to work jointly with the staff of the Office of the Auditor General in the audit of Project financial statements.

Risk Categories	Rating (H, S, M or L)
	As regards limited procurement capacity, the Project, through the financing of non-salary recurrent costs, targets government procurement practices as a key area to be strengthened. This will require: (a) issuing interim instructions as a basis for regulating public procurement until a procurement law is in place, as well as providing orientation and training to the users; (b) drafting of a public procurement bill that meets international and best fit standards; (c) developing regulations and manuals; (d) hiring of procurement consultants to provide technical assistance to FGS, Puntland and IJA for procurement planning, bid-documents preparation, bid-evaluation, contract management, reporting and capacity-building; and (e) undertaking a survey to ascertain indicative costs for commonly-procured items, and establishing an item master list that would be used by the purchasing module of the FMIS. To deal with fraud and corruption, accounting and reporting on the Project will be done using the government financial management information system that is being implemented with the support of the on-going PFM Strengthening project. The system is expected to account for and generate the necessary reports for Project purposes by using the external assistance fiduciary procedures manual. Citizens and Civil Society Organizations (CSOs) will also be asked to monitor the progress of reforms and thereby strengthen public oversight. However, this will take some time as they are likely to face resistance because of the ingrained culture and behavior patterns, and political structures. Lastly, the Oversight Committee (OC) brings together the senior PFM actors to objectively review progress reports and provide managerial direction with direct reporting to the Presidency. Clear criteria for the selection of staff for the RCRFP Phase II Project in the FGS, Puntland and IJA, and the use of annual performance evaluation, will ensure that the right people are selected for the job. The payroll has grown by about 100 percent since the RCRFP started in August 2014. The processing of salaries in the civil service commission is still a fully manual process. The envisaged support for process and technological development has not materialized, and, thus, the process is still on a shoestring. Risks are high. As a result, a more in-depth review and intense time commitment is required for the monitoring of the salary payments.
7. Environment and social	Risks posed to the Project by environmental and social conditions, and the potential, unintended consequences of Project activity on physical, biological and cultural resources and on human health and safety is **Low.** Works to be carried out under the Project are expected to have no, or negligible, environmental impacts as these will be confined to existing buildings, be simple and non-hazardous in nature, and restricted to very basic, small- scale refurbishment of existing buildings of the FGS, Puntland and the IJA governments. While the Project is expected to have positive social impacts through improved confidence in government, resistance is expected from certain public officials who wish to maintain the *status quo* of less-transparent systems and procedures for the sake of their

Risk Categories	Rating (H, S, M or L)
	personal gains. Political and clan-based competition will also mean that procurement opportunities could be divisive and cause conflict. The Project can have unintentional, negative consequences on local power dynamics, if one group is favored over another through the allocation of Project resources. This particular challenge will be addressed by ensuring clear criteria for the selection of Project staff. Appropriate change management and information, education and communication strategies will be adopted. Quick-wins will be pursued to demonstrate the benefits of the reforms. The reform approach will be participatory and will seek to build coalitions that can support change and reform even if the political leadership changes. The project team will monitor the potential impact of activities on power dynamics and conflict drivers, taking care to implement the Project through a conflict-sensitive approach. Deliberate efforts also will be made to utilize an inclusive approach to capacity-building and institutional strengthening to ensure gender balance.
8. Stakeholders	Risks related to stakeholders who might delay or halt activities and may affect successful Project implementation and completion are **Substantial**. PFM reforms in general, and, specifically, civil service salary payments systems reforms, will involve changes that will affect the interests of stakeholders. There will be ***'win–lose'*** situations where the vested interests of respective parties are incompatible, or where other stakeholders cannot, or will not, accept a common position. Understanding the relative power and influence of stakeholders will help to reconcile their claims on the Project. Obtaining a broad consensus for the reforms will ensure sustainability and this requires accepting that all stakeholders are important but different and must be managed differently. Depending on their relative power, importance and influence, Project coordinators in FGS, Puntland and IJA PFM will build a *coalition of change agents* by adopting various communication and participation methods designed to inform, consult, involve, collaborate or empower. Key constituencies such as parliamentarians, the media, CSOs, think tanks and academia will be engaged by involving them through strategic communications using radio and TV discussions. In circumstances where there are significant conflicts of interest, the Oversight Committee will draw on political power from the Presidency. The implementation of reform will be incremental and gradual so that stakeholders are not overwhelmed.
9. Other (Security)	There are additional context-specific risks that are not captured in the other categories. These risks are **High**. In the context of Somalia, security risks will always be included in project-level risk management frameworks. High insecurity poses a risk to Bank staff and clients, and to Project implementation and sustainability. It creates severe limitations of access to the operating environment and, in turn, this elicits a number of additional risks that are challenges to Project implementation and monitoring. The spate of recent bombings in Mogadishu, some close to Villa Somalia and targeting government officials and legislators, will discourage consultants to accept assignments in Mogadishu and even in Puntland and the IJA, and thereby slow down the pace of reform implementation. High security costs will increase significantly the overall cost of the reforms.

Risk Categories	Rating (H, S, M or L)
	The Bank team will operate under the corporate security guidance of the Goods and Services Department (GSD) and under the UN umbrella provided by the department of safety and security. An arrangement is under discussion with a third party firm to which risk can be transferred when hiring Bank consultants. These arrangements are widely in place for other UN agencies.[29] In addition, GSD will hire a security agent to help manage the day-to-day missions of World Bank staff to Mogadishu. The security/logistics firm hired by MOF, as well as the one hired by the Bank will provide reasonable security for an in-country presence to implement the Project. Challenges to state authority by Anti-Government Elements (AGE) could delay or block Project implementation. Moreover, such challenges run the risk of undoing progress achieved through the RCRFP Phase I project and other associated MPF-financed projects. The CMU will monitor the political and security environment, in collaboration with United Nations Department for Safety and Security. In the case of acute political crisis or breakdown, the project will need to be put on hold and potentially be discontinued, based on the severity of the situation.
10. Overall	**The overall risk rating for the project is High**. The government is unfamiliar with World Bank operating and fiduciary requirements and has weak capacity to manage projects. The history of bad governance and corruption risks are high, but the government has so far expressed desire that going forward it will not be "business as usual." Somalia is a high-risk environment and careful management of risks is required. Major country risks include the overall security situation, with incessant instability and the volatile security situation of an active insurgency being led by Al-Shabaab. This could have a number of direct and indirect impacts on the Project, ranging from periodic travel restrictions to a direct attack by Al-Shabaab on government institutions- including the CBS, which is the primary pay-point for civil servants. The Project will mitigate these risks by taking account of the regular security advisories issued by the World Bank and UN, and by relying heavily on the more flexible security arrangements and access arrangements used by the Independent agent to ensure that Phase II Project implementation can continue when staff travel is restricted. The Project will also rely on the security measures that the FGS has taken to protect the CBS and other core PFM institutions from attack.

[29] Based on World Bank security guidance, Bank staff and consultants are currently permitted to travel to the airport in Mogadishu. Movement to Villa Somalia is permitted on a case by case basis depending on mission criticality and the security situation at that time.

SOMALIA: Recurrent Cost and Reform Financing Project: Phase II

Annex 5: Support Strategy and Implementation Action Plan

1. **Implementation Support Plan:** The strategy for implementation support is tailored to the implementation capacities of FGS, Puntland and IJA and has been formulated based on the nature of the Project and its risk profile. It aims to make implementation support to the client more flexible and efficient, and mitigate the risks identified in the SORT.

2. The World Bank team will support implementation through the following activities:

(i) Involvement of World Bank staff, including those from the Governance, Education, Health, Finance and Private Sector Development, and those from Macro-fiscal Global Practices (GPs), and Controllers, in order to leverage comparative and complementary skills to provide regular support to the Project on technical matters. The TTL will also oversee the work program of, and work closely with, the technical experts in the FGS.

(ii) Supervision/implementation support missions from Nairobi and/or Washington D.C every six months during the Project implementation period. One of these missions will be undertaken around August or September of each year and will focus on macro fiscal review to determine the specific allocation for each component and activity in the subsequent year of implementation.

(iii) The Implementation support team will consist of: the Task Team Leader; a lawyer; operational project management; monitoring and evaluation personnel; financial management; procurement, payroll/HRM, health, education and banking experts.

(iv) FGS, Puntland and IJA staff who will be implementing the Project will be strengthened through various forms and types of training on World Bank operational guidelines, processes and procedures, financial management, disbursement, procurement, monitoring and evaluation, strategic communications, leadership, social accountability and project management.

(v) There will be close supervision of financial management to ensure that salary payments are made to the relevant civil servants, using a risk-based analysis approach. Procurement supervision will consist of ex-ante reviews of procurement activities of the key contracts with the consulting firms and individuals to be recruited, as well as ex-post review. Progress of procurement based on the Simplified Procurement Plan will be checked regularly.

(vi) An independent agent (IA) will provide quality assurance and due diligence on the salary payments and on the non-salary recurrent cost expenditures that are to be financed under the Project.

(vii) The Bank will conduct an early midterm review after the second year of implementation to review Project progress and agree any necessary restructuring to achieve the development objectives.

3. To accelerate Project implementation, an Implementation Action Plan has been agreed with the FGS, Puntland and IJA (see Annex 5).
4. The following skills-mix is required for implementation support:

Table 18: Skills Mix for Project Implementation

Skills needed	Number of Staff Weeks per year	Number of Trips per year	Location
1. Adenike Oyeyiola Senior Financial Management Specialist (Task Team Leader, GGODR)	12	6	Washington D.C
2. John Randa Senior Economist (Co Task Team Leader, GMFDR)	8	4	Nairobi
3. Thilasoni Benjamin Musuku Senior Financial Sector Specialist, GFMDR	3	2	Washington D.C
4. Stephen Mugendi Mukaindo Counsel (LEGAM)	1	1	Nairobi
5. Winston Cole Senior Financial Management Specialist (GGODR)	2	2	Dubai
6. Leonard Mutuku Matheka Financial Management Consultant (GGODR)	4	4	Nairobi
7. Christiaan Johannes Nieuwoudt Finance Office (CTRLA)	2	1	Nairobi
8. Anjani Kumar Senior Procurement Specialist (GGODR)	2	2	Juba
9. John F. A Etidau Procurement Consultant (GGODR)	4	4	Nairobi
10. Hugh Riddell Representative (AFCE4)	1	2	Nairobi
11. Ikechi B. Okorie Senior Operations Officer (GGODR)	2	1	Washington D.C
12. Geoff Handley Extended Term Consultant (GGODR)	4	2	Nairobi
13. Huihui Wang Senior Economist (GHNDR)	3	2	Washington D.C
14. Wolfhart Pohl Senior Environmental Specialist (AFTSG)	1	1	Washington D.C
15. Nalin Jena Senior Education Specialist (GEDDR)	3	2	Nairobi
16. Marie Bolou Senior Operations Assistant (GGODR)	4	1	Washington D.C
17. Salome Awuor Aganda E T Temporary (AFCE4)	2	1	Nairobi based

Partners

Name	*Institution/Country*	*Role*
1. Lervåg Astrid	Norway, Astrid.Lervag@mfa.no	Co-chair PSG 5 WG
2. Alessia Riccardi	Desk Somalia, Development Cooperation Office Embassy of Italy, somalia.nairobi@esteri.it	Co-chair of PSG 5 WG
3. Rowan Yamanaka	United Kingdom, DFID	PSG 5
4. John Wearing	j-wearing@dfid.gov.uk	Co-Chair PSG 5 PFM sub-group
5. Katarina Motoskova	Delegation of the European Union to Somalia katarina.motoskova@eeas.europa.eu	PSG 5
6. Per Karlsson	Somalia Section, Embassy of Sweden per.h.karlsson@gov.se	
7. Victor Ndisale	African Development Bank (AfDB) v.ndisale@afdb.org	
8. Albert Soer	UNDP Albert.soer@undp.org	
9. Anka Kitunzi	UNCDF Anka.kitunzi@uncdf.org	
10. James Mugambi	UN-HABITAT, James.Mugambi@unhabitat.org	
11. Tye Ferrell 12. Julie Limoges	USAID tferrell@usaid.gov US Embassy	
13. Liisamaria Keates	Embassy of Finland liisamaria.keates@formin.fi	Counsellor
14. Ivan Parks	Somalia Stability Fund i-parks@dfid.gov.uk	Head, Somali Stability Fund
15. Alan Pearson	Somali Stability Fund	

Table 19: Implementation Action Plan

Activities	**Expected Results**	**Responsible Actor**	**Implementation Date or Estimated date after Approval**
Work plan, budget, and procurement plan.	Work plan and procurement plan validated	WB/FGS, PL, IJA	Done
First quarterly progress report	Report disclosed	WB/EAFS	October 15, 2015
Second quarterly progress report	Report disclosed	WB/EAFS	January 15, 2015

SOMALIA: Recurrent Cost and Reform Financing Project: Phase II

Annex 6: RCRF Phase I: Performance and Achievements

Project Launch and Training

1. The first training of the government team, which also doubled as the project launch, was organized in Nairobi between September 22 and 26, 2014. The training involved thirty-three government staff and was aligned to the provisions of the existing EAFS manual, the SFMIS and World Bank fiduciary and operational requirements. The overall objective of the training was to strengthen the capacity of the EAFS and the MOF in the areas of financial management, procurement and disbursements and introduction to World Bank operations; and to equip the participants with the requisite knowledge and skills, and provide better understanding on the fiduciary requirements of World Bank assisted projects. In particular, the training was customized to address specific fiduciary aspects related to the RCRFP with specific focus on key aspects of EAFS/RCRFP financial management, procurement, disbursements, functional appreciation of the SFMIS and an overview of World Bank operations.

2. The training was undertaken with great collaboration from the PFM Strengthening Project team and facilitated by Bank staff and consultants.

Component 1: Emergency support of core government functions in MDA.

3. **Eligible civil servant salaries in non–security sectors:** Under this sub-component, it was originally planned that the Project would support the FGS to maintain core government functions by financing the salaries of about 3,900 non–security sector civil servants from July to December, 2014 at a monthly estimated cost of US$1,911,667 based on FGS 2014 projections. The target was revised downwards to 3,600 in December 2014 during the Project restructuring exercise.

4. The number of paid civil servants under the Project rose from the baseline of 1,970 in June 2014[30] to 3,687 in December 2014 with an increase in the MDA coverage from 32 to 42 institutions. This represents a growth of eighty-seven percent (87 percent) of the government payroll eligible for payment under the RCRFP.

[30] As of June 2014, salaries had been paid up to the month of February 2014 for 1,970 eligible civil servants under the Norway Special Financial Facility. Salary payments for March to June 2014 were outstanding.

Table 20: **Salary payments during the Project period: July, 2014 – February, 2015.**

Date	Registered civil servants	Ccivil servants presented to CBS for payment			Number of civil servants paid by CBS	Staff who did not claim salaries		Number of civil servants in the register, but not authorized for payment
Month	No.	No.	US$	Date payment started	No.	No.	US$	No.
July 2014	3,404	2,562	1,267,883	Sept 6, 2014	2,515	47	26,469	842
August 2014	3,541	2,579	1,267,883	Sept 23, 2014	2,494	85	53,816	917
September 2014	3,830	2,898	1,449,832	Oct 23, 2014	2,815	83	49,616	932
October 2014	4,012	3,517	1,787,301	Nov 25, 2014	3,517	162	98,111	495
November 2014	4,012	3,671	1,889,188	December 24, 2014	3,483	188	110,047	341
December 2014	4,012	3,687	1,898,284	Jan 6, 2015	3,548	139	80,360	325
January 2015	4,012	3,907	2,023,665	March 10, 2015	3,777	130	75,262	105
February 2015	4,040	4,040	2,078,659	April 27, 2015	3,893	147	81,852	0

5. The Administration of salaries is being guided by a policy and procedures that have been developed by FGS as shown in **Box 1**.

1. **Box 1. Administration of the payment of eligible civil servant salaries**

Salaries eligible for reimbursement under the RCRFP will be available for collection by individuals at the CBS for a period of three months. This period is measured from the first day that pay was available to any civil servant for the relevant period (the "first payday").

Process:

1. The gross salary for the monthly payroll authorized by the Accountant General is transferred from the RCRFP designated account to the FGS Treasury Single Account.

2. The CBS pays civil servants over a six working-days period (subject to change based on the number of civil servants to be paid and possible changes in CBS capacity).

3. The CBS produces reports of those paid and those unpaid ten days after the first pay day ("day ten").

4. RCRFP SOE are prepared based on the report from day ten. Only amounts (gross, including tax) for civil servants who have been paid are claimed for reimbursement under the RCRFP.

5. Amounts (gross, including tax) for civil servants who did not collect their pay are held in the Treasury Single Account for a period of three months from the first payday. These are liabilities of the FGS which will be either:

   a. Paid to the civil servants who did not originally collect their pay but collect this at a later date; or,

   b. Repaid to the RCRFP Designated Account.

6. Amounts paid to individuals who collect their salary between day ten and three months after the first payday will be claimed for reimbursement on the next SOE to be submitted.

7. Amounts held by the FGS in each month for civil servants who did not collect their salary are presented on each DA Reconciliation Statement. These amounts are repaid to the RCRFP DA three months after each first payday.

Financing of Subject Matter Experts (SME) and allowances:

6. All ten SME have been cleared by the Bank and have been confirmed for payments under the RCRFP based on the terms of their on-going contracts with the government. The related SME are three SME in the Prime Minister's office; and SME for procurement, debt management, Inland Revenue, customs, budget, CBS and the auditor general. New contracts were entered into for six months from July to December 2014 to be financed under the RCRFP. The total contract sum is about US$450,000.

7. The allocation of US$360,000 for SME under the planned Capacity Injection Project was not applied because the project was not effective.

Financing eligible non-salary recurrent cost expenses for 4 MDA:

8. This activity was not carried out. Government was late in setting up a payment system reform task force who, amongst other activities is tasked to set up systems for approval of non-salary recurrent costs and lay out criteria for eligible expenditures in this category. This was a prerequisite for reimbursement. The payment system reform taskforce consists of the director general of finance, the accountant general, budget director, PFM coordinator, chief of staff to the Minister, and a senior advisor. The payment system reform defines the payment process and associated criteria, which must be met before expenditures in this category can be considered eligible for reimbursement. This will include ex ante controls, and clear separation of roles between commitment, procurement and payment authorization and execution.

Key Activities for Component I

- Payment of civil servants salaries from July 2014 to February 2015;
- Payment of salaries and allowances for SME from July 2014 to April 2015;
- Production of a report by the Payment System Reform Task Force, establishing systems for approval of non-salary recurrent costs and designating criteria for eligible non-salary recurrent cost expenses for 4 MDA;
- A policy note recommending the holding period for unclaimed salaries was drafted and submitted by the government to the World Bank for its consideration;
- Development of guidelines for the financing of non-salary recurrent cost expenditures.

Component 2: Strengthening systems for expanded operations and service delivery

10. **Expanding support for recurrent cost expenditures to other regions (Puntland and the IJA):** This activity was completed in December 2014 and a stakeholder workshop was organized in Mogadishu in February 2015 for verification and dissemination of the report.

11. S**trengthening support to the social sectors (education and health):** A consulting firm was engaged to carry out the review. This formed the basis for the support under Phase II of the Project.

Component 3: Project management and coordination

12. Consultants were engaged to support the EAFS consultants' Project implementation. An external auditor has been engaged to audit the Project and the audit is on-going. A vehicle was procured for the Project Management Coordination Unit. Thirty-three government staff from the MOF (External Affairs Fiduciary Unit) and Procurement Unit was trained on Bank operations, financial management, procurement and disbursements (paragraph 1). The training also included an exposure of the trainees to the SFMIS. A consultant was engaged to review and prepare a Project completion report.

CHALLENGES

13. The overall risks identified in the Project documents are still valid. Specific challenges are:

(a) There is still a delay in processing reimbursements for the salary payments. EAFS has developed close working relationships with the various government institutions, including the CBS, civil service commission, and the line-ministries, and it is hoped that this will allow FGS to process civil servants' salaries and allowances without major hindrances and in a timely fashion;

(b) Absence of criteria for approving eligible non-salary recurrent cost expenditures for the stipulated 4 MDA caused significant delays in undertaking the activity. While the guidelines and criteria are now agreed (Annex 7), no disbursement was made under this activity at Project completion.

(c) The use of SFMIS for Project transactions has been significantly delayed and challenging. However, the SFMIS was fully rolled out and used to process the February 2015 salaries. The expectation is that the Project transaction will be fully effected with the SFMIS under this phase II Project.

14. **The main issues identified in the Bank's monthly review of payroll and withdrawal applications are:**

a. **Identical names:** There were several cases of identical names in the payroll but with different identification numbers either in the same MDA or across other MDA. The Monitoring (MA) advisory report for November 2014 indicates there were still 96 civil servants or 44 pairs found to have identical names. A physical staff verification and staff count is required.
b. **Entry and exit from payroll:** There were some civil servants that exited and then entered again into the payroll of civil servants across the months and sometimes under different MDA. A further review and/or explanation is required to establish the rationale for the entry and exit. Physical verification of employment records and staff is advised.
c. **Inconsistent in giving allowances:** There were inconsistencies in giving allowances to the civil servants. Some staff within the same grade received allowances while others did not. Similarly, in some instances, staff in different grades received the same allowance while there were different allowances for staff within the same grade in other instances. Also, allowances were not given to some staff of higher grade while some staff of lower grade earned allowances. There is need for harmonization of grading and allowances through policy guidelines.
d. **Unpaid salaries:** A number of civil servants fail to collect their salaries each month on the scheduled days. The number of unpaid salaries was still very high. Civil servants that failed to collect their salaries were about 130 for each month. Reasons for non-collection of salaries need to be established staff by staff month by month
e. **High payroll additions and exits:** Civil Service additions and exits from the payroll were high. In January 2015 the net change in civil service was 286, bringing the total number of civil servants enrolled in the program to 3,907. While this does not exceed the maximum number of eligible civil servants envisaged under phase 1 of this Project which is 3,909, the monthly increase is an issue of concern.

f. **MA monthly report:** There is a delay in submission of the monthly report to the World Bank. For example, payments for the November 2014 salaries were made by FGS in December 2014. However, the MA's report was submitted in February 2015. A timely review and submission of report is critical, as important issues identified in the report could be addressed immediately.

g. **Ineligible commissioners:** 66 commissioners from 3 MDA, the National Civil Service, the National Reconciliation Commission and the National Constitution and Federal Affairs were identified as not eligible for salary payments from the RCRFP Project. While the issue was raised in the MA advisory report for October 2014, FGS continued to pay the salaries to the commissioners in November and December 2014. By the December 2014 payroll, a total of US$155,777 was due for refund to DA by FGS for ineligible salary payments to the commissioners in the months of October, November and December 2014.

Guidelines on administration of salaries not paid during the initial payment period

14. Civil servants are paid in cash at the CBS. The payments are made over several days for each monthly payroll. Each month there are individuals who do not pick-up their payments during the assigned days. A policy and process have been developed by the FGS in this regard:

15. **Policy**: Salaries eligible for reimbursement under the RCRFP will be available for collection by individuals at the CBS for a period of three months. This period is measured from the first day that pay was available to any civil servant for the relevant period (the "first payday").

16. Process:

a. The gross salary for the monthly payroll authorized by the Accountant General is transferred from the RCRFP DA to the FGS Treasury Single Account.

b. The CBS pays civil servants over a six-working days' period (subject to change based on the number of civil servants to be paid and possible changes in CBS capacity).

c. The CBS produces reports of those paid and those unpaid ten days after the first pay day ("day ten").

d. RCRFP Statements of Expenditures (SOE) are prepared based on the report from day ten. Only amounts (gross, including tax) for civil servants who have been paid are claimed for reimbursement under the RCRFP.

e. Amounts (gross, including tax) for civil servants who did not collect their pay are held in the Treasury Single Account for a period of three months from the first payday. These are liabilities of the FGS which will either be: (a) paid to the civil servants who did not originally collect their pay but collect this at a later date; or (b) repaid to the RCRFP DA.

f. Amounts paid to individuals who collect their salary between day ten and three months after the first payday will be claimed for reimbursement on the next SOE to be submitted. Amounts held by the FGS for civil servants who did not collect their salary are presented on each DA Reconciliation Statement by month. These amounts are repaid to the RCRFP DA three months after each first payday.

SOMALIA: Recurrent Cost and Reform Financing Project: Phase II

Annex 7: Eligibility Criteria for Financing of Non-Salary Recurrent Costs

Non-salary recurrent cost expenditures are **operations costs,** including: rent, petrol, oil and lubricants; repair and maintenance of vehicles and equipment; office materials; travel of civil servants and equivalent personnel; training expenses; and utilities. These are referred to as "use of goods and services" in the government budget. The procurement of these goods and services requires strong controls in the process, procurement and confirmation of the actual expenditures incurred.

The Project will ensure that, with respect to this non-salary recurrent cost expenditure, the following guidelines will be used as eligibility criteria:

1. Expenditures must be for non-salary recurrent costs as defined as 'Use of goods and services' in the respective governments Appropriation Act.

2. Expenditures must be charged to the budget of the respective Ministries, departments and agencies (MDA) that incurred such expenditures.

3. To be eligible, expenditures must be incurred during the period beginning from Project effectiveness and ending on the last day of Project implementation.

4. To be eligible, the procedure as prescribed in the Implementation Manual of the Project should be followed to acquire such goods and services.

5. Costs eligible for reimbursement are, per MDA and per expenditure type, within the respective governments' annual budget as amended; and the RCRFP budget as presented in the grant agreement and as prescribed by any further amendments.

Detailed description of these guidelines are in the project operations manual.

Annex 8: Map of Somalia