A NEW INSTRUMENT TO ADVANCE DEVELOPMENT EFFECTIVENESS:

PROGRAM-FOR-RESULTS LENDING

REVISED CONCEPT NOTE

Investment Lending Reform
Operations Policy and Country Services

February 23, 2011

ABBREVIATIONS AND ACRONYMS

AFR	Africa Region
BP	Bank Procedure
CCTs	Conditional Cash Transfers
CAS	Country Assistance Strategy
CODE	Committee on Development Effectiveness
CPS	Country Partnership Strategy
DLI	Disbursement-linked indicator
DPC	Development policy credit
DPL	Development policy lending
EAP	East Asia and Pacific Region
ECA	Europe and Central Asia Region
EEP	Eligible expenditure program
EFA FTI	Education for All—Fast-Track Initiative
FM	Financial management
GAVI	Global Alliance for Vaccines and Immunization
GPOBA	Global Program on Output-based Aid
IBRD	International Bank for Reconstruction and Development
IAD	Internal Audit Department
IDA	International Development Association
IEG	Independent Evaluation Group
IL	Investment lending
INT	Institutional Integrity Department
IP	Inspection Panel
ISR	Implementation Status and Results
LCR	Latin American and Caribbean Region
M&E	Monitoring and evaluation
MCC	Millennium Challenge Corporation
MNA	Middle East and North Africa Region
OECD-DAC	Development Assistance Committee of the Organisation for Economic Co-operation and Development
OBA	Output-based aid
OP	Operational Policy
OPCS	Operations Policy and Country Services
P4R	Program-for-results lending
PESP	Punjab Education Sector Project
PFM	Public Financial Management
PID	Project Information Document
RBFH	Results-based financing in health
SAI	Supreme audit institution
SAR	South Asia Region
SEP	Sindh Education Sector Project
SIL	Specific investment lending
SWAp	Sectorwide approach
UNICEF	United Nations Children's Fund
WHO	World Health Organization

A New Instrument to Advance Development Effectiveness: Program-for-results Lending Revised Concept Note

Contents

Boxes and Table

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EXECUTIVE SUMMARY

1. World Bank Management is proposing a new Program-for-Results (P4R) lending instrument to respond to changing development needs and demand from borrowing countries. P4R would focus Bank support directly on improvements in sectoral or other development programs and would place more direct emphasis on results by making them the basis for disbursement. It would focus Bank technical and financial support more strongly on institutional development, particularly capacity to monitor results and strengthening of the country expenditure systems. It would also enable the Bank to leverage its own financing and collaborate with other development partners through pooling resources and focusing efforts on supporting government programs. With its program-level orientation, the new instrument would complement the Bank's two existing lending instruments—investment lending (IL), which supports specific projects and disburses against specific transactions, and development policy lending (DPL), which supports policy and institutional reforms.[1]

2. ***IL Reform.*** The proposal to introduce a new program lending instrument emerged from the Bank's IL reform process. As part of the IL reform progress report to the Committee on Development Effectiveness (CODE) in March 2010, Management indicated its intention to propose such an instrument. CODE expressed support for the instrument's focus on a "program-based" approach as a complement to the "transaction-based" approach of traditional IL. In October 2010, Management provided CODE with an initial draft of a concept note for the new instrument. CODE supported the broad directions proposed in the note and requested additional details—particularly with respect to the rationale for a new instrument separate from IL and DPL, the definition and treatment of results and their links with disbursements, the assessment approach for procurement and environmental and social impact and risk management , and the name of the proposed instrument. This revised concept note responds to that request and provides further details on the proposed new instrument.

3. ***Key Features.*** The key features of the proposed new instrument would be as follows:

(a) ***Finances specific sectoral or subsectoral expenditure programs.*** Disbursements would finance defined borrower expenditure programs designed to achieve specific results. Disbursements would not be attributable to individual transactions.

(b) ***Disburses upon achievement of results and performance indicators, not inputs.*** Disbursements would be determined by reference to progress on monitorable performance indicators, rather than simply by whether expenditure had been incurred.

(c) ***Focuses on strengthening the institutional capacity that is essential to ensuring that the programs achieve their expected results and can be sustained.*** A priority area for both preparation and implementation support would be to strengthen the institutional

[1] In addition, the Bank also offers Guarantees in the context of the mobilization of private sector finance.

capacity of the country's own systems, and thereby to enhance development impact and sustainability.

(d) ***Provides assurance that Bank financing is used appropriately and that the environmental and social impacts and risks of the program are adequately addressed.*** The program would be monitored to ensure that loan proceeds are used for program expenditures and that these expenditures are incurred with economy and efficiency. The program would also ensure that an adequate system is in place to protect affected people and the environment.

4. ***Use of P4R.*** The proposed new P4R instrument would provide client countries with a wider range of instruments to choose from, depending on the nature of the support they are seeking, the risks, and the desired results. DPL would remain the primary Bank instrument to support policy and institutional actions to achieve a country's overall development objectives, with rapidly disbursing general budget support to help address development financing needs. IL would remain the Bank's main instrument to support projects, with disbursement against specific expenditures and transactions. P4R would be the instrument of choice when the objective is to support the performance of a government program using the government's own systems; when the results require expenditures; and when the risks to achieving the program's objective relate to the capacity of the systems to achieve better results, including with respect to fiduciary and environmental and social issues. It is intended that the P4R instrument would be available to a broad range of countries, sectors, and programs particularly since the P4R is an instrument to support institutional development and capacity building, including in low income and low capacity settings. However, the use of the instrument would differ significantly depending on the strength of the institutional environment. As P4R is positioned between DPL and IL, it will build on the lessons learned from both instruments and combine proven elements of existing instruments in a way that makes them more effective for supporting country programs and institutions.

5. ***Next Steps.*** The new instrument provides a major opportunity for the Bank to enhance its development impact. But it also poses important challenges and risks that need to be addressed during the instrument development and consultation phase. This note identifies some of these risks and proposes ways to mitigate them. It is intended to facilitate broad-based consultations within the Bank, with Executive Directors, with external partners, with client countries, and with civil society organizations and other stakeholders. Feedback from the consultations would be reflected in the final design, including the Operational Policy/Bank Procedures (OP/BP) statements, legal agreements, management information systems, and guidance and training materials for staff. The final details of the new instrument—including a proposal for enhanced management oversight arrangements for an initial period following the introduction of the instrument—would be brought to the Board for discussion and approval by the end of FY11.

PROGRAM-FOR-RESULTS LENDING
REVISED CONCEPT NOTE

I. INTRODUCTION

1. In February 2009, Bank Management presented to the Board a Concept Note[1] that set out the process by which Management proposes to transform investment lending (IL) to achieve greater development effectiveness through a stronger focus on results. The note indicated that the work would be organized around five pillars or components: adoption of a risk-based approach for processing IL; greater emphasis on supervision and implementation support; a consolidated and rationalized menu of financing options for IL; actions to provide an enabling environment for supporting and reinforcing the implementation of the reforms; and simplification and revision of the policy framework. In October 2009, Management reported on the first two pillars—the proposed risk framework and implementation support—to the Executive Directors, who broadly welcomed and accepted the report.[2]

2. ***Initial Description of a New Instrument.*** In March 2010, Management provided a further update to CODE on progress with respect to IL reform. The update provided specifics on implementation of the first phase (the risk-based approach and implementation support) and also introduced an outline of next steps and the evolving concept for a new lending instrument to support government programs and disburse against results. Management explained that the new instrument was conceived in the context of IL reform but, after careful consideration, would be proposed as an instrument separate from and complementary to both IL and development policy lending (DPL). CODE members welcomed the initial discussion, and expressed their support for the focus on a "program-based" approach as a complement to the "transaction-based" approach of IL. They also commented on the rationale for the new instrument and its expected impact on the way the Bank engages with clients and development partners, the review of defined government expenditure programs, and the fiduciary and environmental and social aspects of such operations.

3. ***Concept Note.*** In October 2010, Management provided CODE with an initial draft of a concept note for the new instrument. CODE supported the broad directions proposed in the note, including the focus on programs and the clear link to results. Members asked for additional details—particularly with respect to the rationale for a new instrument separate from IL and DPL, the definition and treatment of results and their links with disbursements, the assessments of procurement and environmental and social impact and risk management, and the name of the proposed instrument. This revised note responds to these issues.

4. ***Purpose and Structure of this Revised Note.*** Building on the discussion in the two CODE meetings, this revised concept note provides additional details on the proposed new Program-for-Results lending instrument, or *P4R*, which would be designed to support a government's program in particular sectors or subsectors with a clearly defined results framework. The note has been prepared to facilitate consultations and seek guidance prior to

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[1] *See Investment Lending Reform: Concept Note* (SecM2009-0026), January 26, 2009.

[2] See *Moving Ahead on Investment Lending Reform: Risk Framework and Implementation Support* (SecM2009-0442), September 3, 2009.

requesting formal approval for introduction of the instrument. Section II reviews the demand for Bank financing as reflected in country strategies. Section III reports on the Bank's lessons from experience with various IL operations that have programmatic features and link disbursements to results. Section IV presents the rationale for the new instrument. Section V describes the key features and use of the new instrument. Section VI outlines what it would look like, including how critical underpinnings, such as fiduciary and environment and social impact and risk issues, would be approached. Section VII presents some of the challenges and risks to the further development and introduction of the proposed instrument and how they might be addressed, and Section VIII summarizes the proposed next steps. Annex A summarizes some of the Bank's experience with programmatic investment lending, among others, Annex B provides additional details on the technical and systems assessments that would need to be undertaken for P4R, and Annex C presents a summary of the consultation plan.

II. COUNTRY STRATEGIES AND WORLD BANK INSTRUMENTS

5. Over the past decades, as the Bank has sought to better serve its clients by adopting a country-focused approach to providing development solutions, Country Assistance Strategies (CASs) and Country Partnership Strategies (CPSs) have become more aligned with countries' own priorities and development objectives. CASs/CPSs are extensively discussed with concerned governments and other stakeholders before they are finalized, and they provide a clear indication not only of the agreed objectives of the Bank's assistance but also of the range of instruments that the Bank expects to use to realize those objectives.

6. ***Demand for Bank Services.*** A review of the 51 CASs/CPSs discussed by the Board between 2008 and 2010 yields information on country demand for the Bank's lending, advisory, and other services. With respect to lending, almost all the countries covered expect to continue benefiting from traditional IL, while 36 of the 51 countries (69%) expect to benefit from DPL and 34 (65%) request some form of programmatic lending or program-based or sector-wide approach.

7. ***Demand for Programmatic Lending.*** Demand for programmatic lending comes from countries in all income categories, with 15 of 17 low-income economies interested in programmatic lending, 11 of 21 lower-middle-income economies, and 7 of 10 upper-middle-income economies.[3] Demand also comes from all Regions, including Africa, where 15 of the 21 countries reviewed request sector-wide approaches to the Bank's lending activities. Finally, the demand for such lending covers a broad range of sectors—education, health, social protection, roads, water, energy, urban development, and agriculture—and also involves support to states or other lower levels of government.

8. ***Nature of Programmatic Support.*** While there is no standard definition of a programmatic, program-based, or sector-wide approach, countries are generally clear as to what they expect of the Bank. They want a programmatic approach that is integrated, holistic, and focused on performance measurement and results. The programs to be supported need to be owned by the government, aligned with sector and macro priorities, and focused on system strengthening, with the financing of

[3] In addition, the review included 3 high-income economies, only one of which requested programmatic support in the form of sectorwide approaches.

the programs integrated into national budgets. Such approaches should also be used as a mechanism for better coordinating the support of all external partners, including through possible joint funding.

9. ***Summary.*** This review of CASs/CPSs shows that Bank member countries are seeking three types of financial support from the Bank: support for specific projects; support for major policy and institutional reforms; and support for strengthening of ongoing and new government programs in a broad range of sectors to achieve desired results.

III. EXPERIENCE WITH PROGRAMMATIC OPERATIONS[4]

10. While the Bank has never had a stand-alone program-based lending instrument under a dedicated policy framework, features of programmatic lending have been used in operations approved and implemented over more than a decade. A review of experience with these operations provides some perspective on how the Bank has been responding to the high level of demand for these types of operations (Annex A provides additional detail). Whenever these features have been used, the essential nature of the IL product has been preserved—investment in nature, a focus on tangible results, financing expenditures of the borrower, and maintaining the objectives and overall standard of Bank fiduciary and environmental and social safeguards work.

A. Summary of Experience

11. ***Programmatic Features are Not New.*** Many of the operations with programmatic features have their roots in what has come to be known as "program-based approaches."[5] These operations have evolved in profile since the 1990s in response to a stronger focus on results and to clients' increasing demand for support of government programs and assistance in addressing system-level weaknesses. Vehicles used have included sector-wide approaches (SWAps), conditional cash transfers, the Global Program on Output-based Aid, the Results-based Financing in Health initiative, and the Education for All Fast-Track Initiative. It is noteworthy that the demand for such programs and operations comes from both middle- and low-income countries, and covers a broad range of sectors. Box 1 provides an example of programmatic lending for the education sector in Pakistan.

12. ***Implementation Record is Good.*** Reviewing the overall performance of programmatic ILs is complicated by the fact that these operations are not separately coded and can therefore be difficult to identify. A sample of around 40 such projects identified by the Regions[6] revealed that they perform at least as well as the overall IL portfolio; and a more recent analysis of SWAps, conditional cash transfers, and output-based aid confirms that their project performance

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[4] The review of World Bank supported projects with programmatic features was limited to investment lending operations.

[5] There is no single definition of a program-based approach. The most commonly used description is the OECD-DAC's: "A way of engaging in development cooperation based on the principle of coordinated support for a locally owned program of development. It includes four elements: leadership by the host country organization; a single program and budget framework; donor coordination and harmonization of procedures; and efforts to increase the use of local procedures over time with regard to program design and implementation, financial management, and monitoring and evaluation."

[6] The review included operations from all Regions (13 from AFR, 3 from EAP, 4 from ECA, 12 from LCR, 3 from MNA, and 6 from SAR_ that covered education, health, other social sectors, infrastructure, local government/urban, finance, and multi-sectoral programs. The total lending volume was US$9 billion.

indicators compare favorably with those of the overall lending portfolio. These types of operations appear to have a stronger results orientation, at least in part because several of them include disbursement-linked indicators (DLIs). Implementation Status and Results (ISR) reports rated monitoring and evaluation as moderately satisfactory or better for 90 percent of these projects by number and 97 percent by value. The types of results have varied and (like other aspects of program design) have been tailored to the development stage of the supported government program and its expenditures. At the same time, staff report that the continued process- and input-intensity of the IL product displaces time from focusing on substantive results, and that internal processing is their greatest difficulty.

Box 1. Programmatic IL: The Experience in Pakistan

The Punjab Education Sector Project (PESP) and Sindh Education Sector Project (SEP), approved by the Board in June 2009, use an IL instrument with programmatic features to support education reforms in their respective provinces. These projects built on the experience of projects in LCR: Minas-Gerais Partnership II SWAp and Ceara Multi-Sector Social Inclusion Development in Brazil. Minas supported five sectors, including health and education, and Ceara supported human development and sustainable resource management. The Pakistan teams, learning from the LCR operations, designed specific IL credits to support the governments' programs for primary and secondary education. The projects disburse against eligible expenditure programs (EEPs) based on the achievement of predetermined disbursement linked-indicators (DLIs). The DLIs include intermediate outcomes, implementation performance/institutional change indicators that build incrementally over the life of the project.

Evolution of support. The Bank previously engaged the education reform programs in Punjab and Sindh through development policy credits (DPCs) that supported policy reforms in the sector. The program then followed up with a specific investment credit building on the achievements of the DPCs while focusing on implementation outcomes and outputs through the achievement of measurable targets (DLIs). The new approach also provided enhanced focus on strengthening associated provincial systems (e.g., fiduciary, safeguards, and monitoring and evaluation, or M&E) through technical capacity building and implementation support.

Flexibility in design. The flexibility in the design allowed the Bank to support a part of the government's program and priorities while maintaining a strong focus on the achievement of key results. The DLIs were determined in partnership with the provincial governments, reflecting priority elements in the provincial reform programs. This also allowed for the DLIs to be tailored to the specific needs in each province.

Focus on governance and M&E. The use of this lending approach facilitates an emphasis on governance improvements by targeting subprogram design at strengthening education sector governance and institutionalizing accountability in the delivery of education. Some examples:

- Merit and need-based teacher recruitment in Sindh;
- Implementation of a teacher incentives program in Punjab; and
- Strengthening of school-based management, with establishment and capacity building of school management committees in both Punjab and Sindh.

A strong focus on M&E is also a part of project design to complement governance reform. For example, the government's own M&E systems, such as the annual public school census, have been strengthened and are now used to motivate policy and implementation decisions. Third-party validations are built into project design to evaluate subprogram performance and achievement of DLIs. Lastly, impact evaluations for key interventions are integrated into project design to provide valuable information to inform future program directions and decisions.

13. ***Global Phenomenon.*** The call for more focus on results and for stronger links between financing and results is not unique to the World Bank; other agencies have also been exploring such options. A number of global initiatives have been created to support closer links between funding and results—for example, the Global Fund to Fight AIDS, Tuberculosis and Malaria, the Millennium Challenge Corporation, and the GAVI Alliance (formerly known as the Global Alliance for Vaccines and Immunizations). While the Bank cannot adopt some of these

approaches wholly, they reflect an increased desire by development partners to link resources more directly to results.

B. Current Lending Options

14. The volume of programmatic IL operations has grown significantly in recent years to respond to increasing demand. Its sectoral, regional, and product design profile has adapted and evolved, reflecting considerable innovation to meet different country conditions (client demand, development needs, and institutional arrangements) and to focus more on results. While the growth in demand testifies to the perceived value of these operations, it also reveals an uncoordinated institutional response and the lack of a coherent framework from which all would benefit. A lack of clarity on how to approach and how to interpret the current IL operational framework that was designed for a very different kind of lending has also contributed to a lack of clarity among staff (both those who offer guidance and interpretation and those expected to follow it), clients, and development partners. Moreover, staff often have to revisit the same set of issues for each programmatic IL project, and guidance is not always consistent. This has led to high transaction costs that do not contribute much to the overall development goals and may at times limit the program's achievement of its full potential.

15. ***Application of IL Operational Policies and Procedures.*** One key limitation relates to the application to programs of some of the Bank's IL policies and procedures which was designed for specific ring-fenced projects. Currently, programmatic investment operations have had to be squeezed into the existing IL fiduciary and safeguards policies that are designed for traditional IL projects rather than a results-led program approach. This creates a number of problems and missed opportunities (see Box 2):

(a) It often requires a double layer of controls (to ensure the implementation of activities supported by the operation with respect to the requirements of both the government and the Bank), which can impose additional costs on clients without any perceived additional value.

(b) It has led to project designs that are biased toward activities that are easier to accommodate within the current Bank procedures rather than being primarily driven by delivering maximum results.

(c) Cherry-picking specific activity types under a program limits the ability of the Bank to partner with the client on implementing improvements in the effectiveness and efficiency of the entire program.

(d) Overlaying concerns about the application of Bank rules to a country program and compliance with the Bank's rules has often resulted in key institutional issues receiving less attention than procedural compliance.

(e) Uncertainty about how Bank policies and procedures (including those on procurement and environmental and social safeguards) designed for more traditional IL projects should apply to more programmatic lending has heightened risks for both client countries and the Bank.

Box 2. Using the IL Instrument in India and Brazil: Achievements and Limitations

The ***India PMGSY Rural Roads Project*** (P124639), financed by an IDA credit of US$1 billion and an IBRD loan of US$500 million, is supporting the Government of India's Rural Roads Program, which aims at providing all-season road access to all villages with a population above 500. About 30 percent of India's villages (or 300 million people) are without all-season access to social services and economic opportunities. Launched in 2000, the Government program has already financed the connection of 70,500 villages through 270,000 km of new or improved rural roads, at a cost of US$14.7 billion. It is estimated that another US$40 billion will need to be spent to achieve the program's target by 2020.

Bank financing supports implementation of a time-slice of the program in the seven Indian states where most progress will be needed to achieve the program's targets. Bank funds will be disbursed against results achieved in those states, in terms of enhancing connectivity (another 8,200 villages would be connected), improving effectiveness of public administration (including new, more efficient, countrywide specifications applied to manage rural roads and procure civil works), and maintaining the roads (increased portion of the rural road network under maintenance contracts).

While the program is overall acceptable to the Bank, Government procedures under the program had to be modified to conform to the Bank's IL policies, especially in the procurement and social impact areas. The Bank was able to accept a modified version of the program procedures mainly because the contracts under the program are of low value and complexity and have the potential to generate only small negative impacts on the environment and society. The combination of support to a program of small infrastructure expansion with the use of a modified version of program procedures and of result-based disbursements make this operation one of the frontier Bank IL operations providing programmatic support.

However, this approach came at a cost. First, it led to 'cherry-picking' by excluding all contracts under the Program ongoing at the project's effectiveness, reducing the Bank's ability to positively influence the performance of those contracts. Second, much of the Government and Bank's project preparation resources were spent finding an acceptable way for the Government to conform to prescriptive IL requirements, instead of partnering to achieve further efficiency improvements under the Program, especially in improving cost-efficiency and sustainability. Third, because of the transaction focus of IL policies, the transaction cost of implementation support will be high with over 7,000 contracts expected to be financed under the Project, spread over a territory covering about a third of India.

Under the ***Brazil Minas Gerais Partnership for Development II*** project, cumulative IBRD lending of $1.5 billion, supports the Minas Gerais "State for Results" program, seeking improved public sector management in several sectors and stronger results management by the state government. IBRD resources are disbursed against indicators in six sectors: public sector management, private sector development, health, education, transport, and rural poverty reduction. The operation includes extensive technical assistance, some of it financed under the loan and some provided by Bank staff as part of project support, including in the areas of public procurement and performance-based contracting of infrastructure and services. IBRD provides around 18 percent of program financing. Semiannual disbursements are proportionate to the achievement of indicators, provided that the Government has financed at least 70 percent of total program expenditures.

The project has proven instrumental in supporting the Government in implementing a broad array of reforms and efficiency improvements under 20 government expenditure programs or initiatives. In particular, the project has supported the Government in modernizing fiscal management and improving tax efficiency, introducing a result-based public sector management culture, further involving the private sector in the state's development, improving coverage, quality and efficiency in health services delivery, achieving faster improvement in school quality and education, improving the condition of the state road network, and providing all-weather access to all municipalities in the state.

However, to fit within the parameters of the IL instrument, the Bank had to exclude about 50 percent of the civil works contracts from the program because such contracts, while deemed to follow good procurement practice, did not strictly follow Bank procurement rules. For the same reason, the program could not include any consulting services contracts procured following Government processes. In sum, choosing projects that avoid procurement (and safeguards) for procedural reasons deprives the Bank of the opportunity to support important improvements in both of these critical areas.

16. ***SWAp Experience Demonstrates the Limitations of an "Approach."*** In the past, staff and clients have tried to deal with some of these issues by using a type of programmatic lending generally referred to as SWAps. However, SWAps are, as their name suggests, approaches, not a new way of doing business. As a result, Bank teams have to jump through many hoops to reconcile SWAp objectives with the transaction focus and prescriptive nature of IL policies, as well as with the client's own procedures and processes under the program. In interviews conducted as background for IL reform, a number of Bank teams indicated that they had given up any attempt to develop SWAps because the lack of clarity on how to process such programs made it hard for fiduciary, legal, safeguards, or disbursement staff to respond to the needs of a SWAp. In addition, the SWAp approach has been characterized as costly in time and effort for development partners and countries, making it more difficult to fully capture the benefits of the approach.

17. ***Application of DPL.*** While DPL is an excellent option for supporting policy and institutional reforms, it is not easily applicable to the provision of the medium- and long-term support for system improvements, capacity development, and partnership strengthening. There are core aspects of the type of program support client countries are now requesting.

18. ***Missing Opportunities.*** Perhaps the most important limitation of the existing menu of lending instruments relates to the missed opportunities to achieve a better development impact. While IL and DPL operations deliver much in support of Bank country programs and will continue to be the leading lending instruments, neither fully allow support to be tied to results from specific programs of expenditures. The Bank, therefore, is missing opportunities to partner with clients in improving the efficiency and effectiveness of some of the development programs and thereby enhance its overall development effectiveness. By aligning more of its support directly with government investment programs, focusing directly on systems improvement and capacity building, and working in partnership with governments and other stakeholders to reorient programs to be more results-based, the Bank has the opportunity to further improve its track record of delivering results across a broad range of sectors and countries, and increase significantly the sustainability of its impact.

IV. RATIONALE FOR PROPOSED PROGRAM-FOR-RESULTS LENDING

19. The proposed new lending instrument will help partner countries increase the impact of public expenditures. For the first time, it would formally link disbursements with the results of a specific expenditure program. It would scale-up the Bank's impact and provide for more sustainable results by focusing on broader programs and country institutions. It would also provide a vehicle to deepen the links between the Bank's knowledge and lending products. In the absence of other options, clients and staff have found creative ways to pursue these objectives through programmatic IL. These tried and tested innovations would be codified in the new instrument. However, valuable though these gains have been, they have been applied unevenly by country and sector, and have led to missed development opportunities. By adding P4R and linking its financing to results, the Bank will have on its menu a complete range of tools to address the overall set of development challenges and enhance its overall development effectiveness. Also, since P4R is positioned between IL and DPL, it is able to build on the lessons learned from both instruments.

20. ***Changing Country Engagement Model.*** In proposing a new instrument, Management is responding to changing demand and a changing country engagement model. Client countries are increasingly implementing their own programs for development and poverty reduction. They are asking development partners for finance and expertise to improve such programs' effectiveness and efficiency in achieving results. Because these programs are being implemented in a wide range of institutional settings, a lending instrument to support such programs must be flexible enough to work in different capacity environments. The proposed new P4R instrument would strengthen country institutions by aligning resource transfers with government programs, place more emphasis on countries' capacity to achieve and monitor results, and focus on institutional improvements that would lead not only to better results but also to a more enabling governance environment. It would align the Bank's technical and financial support more strongly on institutional development, capacity building, and implementation support. It would also enable the Bank to more effectively leverage its financing and partner with other development organizations in supporting country programs.

21. ***Need for Another Lending Instrument.*** The Bank needs a suite of lending instrument that responds to three broad sets of demands from clients:[7]

(a) ***Policy support operations:*** operations that support policy and institutional actions to achieve a country's overall development objectives and provide rapidly disbursing general budget support to help address development financing needs;

(b) ***Project support operations:*** operations that support specific investment projects and disburse against specific expenditures and transactions; and

(c) ***Program support operations:*** operations that support government programs or subprograms and system strengthening, and that disburse against results, providing funding for specific expenditure programs.

22. ***Instruments to Respond to Different Development Challenges.*** The proposed new P4R instrument would complement, not replace, existing lending products. Borrowers would be able to choose from a wider range of instruments, depending on the objective, desired results, and risks faced. The description below illustrates the differences and complementarities among the instruments (see Table 1).

(a) ***Development policy lending.*** DPL would remain the primary Bank instrument to support policy and institutional actions. It focuses on discrete policy actions within the direct control of governments, and links disbursements to evidence that those actions have been adopted. DPL is a practical and effective way of supporting the achievement of results when policy actions are critical to creating the enabling conditions for improving results—for example, when new regulations are required for the better functioning of markets or new policy frameworks are necessary to improve government efficiency. DPLs provide general budget support and do not earmark loan proceeds for specific programs. Moreover, DPLs disburse against specific policy

[7] In addition, the Bank also offers Guarantees in the context of the mobilization of private sector finance.

and/or institutional actions and cannot disburse against the results or outputs/outcomes associated with sector/program expenditures.

(b) ***Specific investment lending (SIL).*** SIL is the Bank's main instrument to finance investment projects**.** It supports a heterogeneous range of operations, but their common characteristic is the financing of specific government investment activities that involve a set of expenditure transactions, most of which are used for the purchase of works, goods, and services. SIL operations have proven to be a practical and effective way of supporting the achievement of results when risk mitigation and controls must be placed over inputs (e.g. construction, technology) and when technical design and implementation challenges are critical bottlenecks to achieving results. Without addressing these constraints, results cannot be achieved—and to the extent that technical challenges (at both the design and implementation stage) are addressed, the probability that results will be achieved is very high. Often such situations involve discrete, one-off activities (for example, the construction of a large infrastructure project or the purchase of expensive and technically complex equipment). By focusing on the proper implementation and risk mitigation of individual transactions, SIL operations put the emphasis of Bank-client relations on making sure that the right inputs and technology are in place and are implemented as planned.

(c) ***Program-for-Results.*** P4R would be the instrument of choice when the objective is to support the performance of a government program using the government's own systems, when the results require expenditures, and when the risks to achieving the program's objectives relate to the capacity of the systems to achieve better results, including with respect to fiduciary and environmental and social issues. Many of the development challenges client countries face cannot be addressed just through discrete policy actions or through the proper technical implementation of a project. For example, improving service delivery (e.g., better maintained roads, functioning schools and health clinics, effective agricultural extension services) may well require both policy actions (e.g., a decentralization law) and some discrete investment activity (e.g., constructing new schools or contracting works for road maintenance). But in many cases, these are not sufficient for the achievement of results. Schools can be built, but teachers may remain absent; health clinics may have new equipment, but essential drugs may not be available at the point of service; and rural roads may remain un-maintained in spite of the existence of contracts due to lack of sustained financing. Addressing such bottlenecks involves improvements in systems including capacity building and changes in management practices and behaviors by service providers and users alike. P4R would also enhance the Bank's ability to partner with other development organizations in supporting government programs by pooling resources and focus on capacity building.

Table 1. Complementary Lending Instruments

Category	***Project support lending (SIL)***	***Program-for-Results lending (P4R)***	***Policy support lending (DPL)***
Type of operation	Supports specific investment operations	Supports government programs or subprograms	Supports policy and institutional actions
Disbursement mechanism	Disburses against specific expenditures that support the operation	Disburses upon achievement of results and performance indicators	Disburses against policy and institutional actions
Implementation mechanisms	Bank IL rules and procedures Funds for specific expenditures	Program systems Funds for specific expenditures program	Country policy processes Funds for non-earmarked general budget support

23. ***Distinction Merits Dedicated Instrument and OP/BP.*** The distinct nature of P4R requires a dedicated instrument and associated set of operational policies. IL policies, in general, are prescriptive, transaction-based, and procedural in nature because they were designed to fit a discrete investment project, particularly in infrastructure, in which close attention to the details of how inputs are obtained are critical ingredients to success. They are in many ways detached from the government legal framework; and some assume that the Bank's funds can be segregated from other sources of finance or earmarked for specific expenditures. Under P4R, the activities to be financed support a government development program that may predate Bank involvement, involve other development partners, and will often see Bank funding that may represent only a modest part of the total financing, with all partners endeavoring to rely on and improve the government program's own systems and controls. P4R operations must meet the requirements of the Bank's Articles of Agreement, and a substantive standard in the areas of fiduciary and environmental and social aspects no less than investment lending. However, it is not realistic to require that a larger program, which is to a large extent funded by governments and/or other development partners, follow all the Bank's input-oriented procedural IL requirements. It is therefore necessary to have a dedicated policy statement that maintains, inter alia, the Bank's high standard of fiduciary and environment and social performance adapted appropriately to the more programmatic and results-driven form of engagement presented by P4R. While it is in theory possible to amend the current IL OPs/BPs to create the necessary authorizing environment for P4R, the process would be complicated and time-consuming, and the result may still confuse clients and staff.

24. ***Support of Country Systems.*** P4R would provide the Bank with another platform for supporting the strengthening of country systems. Effective country systems and institutions are fundamental to the Bank's development mission. The Bank has joined developing countries and other development partners in endorsing the Paris Declaration on Aid Effectiveness and the Accra Agenda for Action, which together express the international consensus in favor of strengthening and expanding the use of country systems. P4R provides the opportunity for the Bank to use and thereby strengthen the performance of country institutions responsible for implementation of the program being supported. The introduction of P4R would therefore enable the Bank to focus more systematically on the strengthening of country systems through improving or enhancing government systems at the sector and program levels. The proposed approach to meeting the Bank's fiduciary and safeguards concerns under P4R would focus on an assessment of the adequacy and capacity of program processes and systems, on the improvements necessary to ensure better results, and on what

the Bank can do to help realize such improvements. Implementation support would provide more focused technical advice to improve systems and capacity building to improve performance. While P4R would contribute to the broad agenda of country systems, it would be different from the country systems pilots because it would not seek procedural equivalency to the Bank's policies and procedures designed for IL operations.

V. KEY FEATURES AND USE OF P4R

25. This section highlights the main features of P4R and the factors that would be taken into account when considering whether a government program is suitable for P4R support.

A. Key Features of P4R

26. The new instrument would have four key features:

(a) ***Finances specific sectoral or subsectoral expenditure programs.*** Disbursements would finance defined borrower expenditure programs designed to achieve specific results. Disbursements would not be attributable to individual transactions.

(b) ***Disburses upon achievement of results and performance indicators, not inputs.*** Disbursements would be determined by reference to progress on monitorable performance indicators, rather than simply by whether an expenditure had been incurred.

(c) ***Focuses on strengthening the institutional capacity that is essential to ensuring that the programs achieve their expected results and can be sustained.*** A priority area for both preparation and implementation support would be to strengthen the institutional capacity of the country's own systems, and thereby enhance development impact and sustainability.

(d) ***Provides assurance that Bank financing is used appropriately and that the environmental and social impacts and risks of the program are adequately addressed.*** The program would be monitored to ensure that loan proceeds are used for program expenditures and that these expenditures are incurred with economy and efficiency. The program would also ensure that an adequate system is in place to protect affected people and the environment.

B. Use of P4R

27. The demand for P4R comes from a broad range of member countries, including both low- and middle-income countries, and to support a broad range of program types in many different sectors. As with both DPL and IL, there would be no a priori restrictions on the use of P4R in terms of income categories or sectors. Instead, decisions on the feasibility and scope of P4R would take account of the following considerations.

(a) ***Consistency with CAS/CPS.*** The appropriateness of P4R would be determined in the context of the CAS/CPS and the Bank's overall assessment of the country's policies and programs and its institutional capacity to undertake those programs.

(b) ***Definition of the program.*** Since P4R operations are expected to support new or existing country programs, the Bank would determine whether the program to be supported is included in a country's development strategy and plans. A program could be as large and broad in scope as an entire sector or subsector, or as small and simple in scope as a specific intervention in a particular geographical area. It could also be a "time-slice" of an ongoing program.

(c) ***Constraints to achieving development outcomes.*** Once the program is defined and verified, a determination of the constraints to achieving the development outcomes would be carried out to decide on the appropriate instrument to use. If the bottleneck is one that primarily requires policy or institutional actions, it may be more appropriate to use a DPL. If the key bottleneck is technical, then a focus on managing inputs using the SIL instrument may be more appropriate. For P4R, the implementation challenges would largely be institutional rather than technical, with improved overall program performance demanding a focus on incentives and accountability for results.

(d) ***Exclusion of High Risk Activities.*** Investment, such as those that, if they were supported by IL, would typically be classified as category A or require corporate level procurement reviews, or those with high risk that cannot be mitigated through the operation, would be excluded from P4R support. These would include activities with potentially significant, irreversible negative impacts on the environment and affected people. This criterion is based on those used in the Guidelines for Environmental Screening and Classification for IL category A projects. P4R would also exclude activities requiring high-value and/or complex procurement packages, a criterion that is the basis for corporate level procurement reviews for IL projects. Examples of these exclusions are likely to be found in construction of large scale complex infrastructure or provision of large scale complex IT activities.[8] The detailed design of the instrument will specify in more detail how these two criteria will be applied.

In addition, P4R design would also include a risk assessment framework with the necessary inputs, at project concept stage, to evaluate a program's riskiness, and reject those not suitable for P4R support (see para. 60).

[8] Illustrative examples would generally include new construction or expansion of large and complex ports, airports, railways, highways, bridges, or tunnels; new construction of large dams or power plants; new construction or expansion of major water or wastewater treatment facilities; mining or extractive industries; and supply and installation of complex industrial plants.

VI. DESIGN AND IMPLEMENTATION OF P4R OPERATIONS

28. This section outlines how P4R operations would be designed and appraised, and describes the nature of the implementation support that would be required. It is organized around the key appraisal dimensions, starting with the assessment of the analytic framework and moving on to fiduciary and environmental and social issues. The assessments would examine the program systems in place, their performance and capacity to implement, and the risks of the various aspects of the program. As for IL and DPL, a risk assessment framework for P4R would be designed to help identify risks, assess the risk mitigation measures, and determine the level of management oversight. Annex B provides additional details on the technical and systems assessments that would need to be undertaken for the P4R.

A. Technical Assessment

29. How would programs supported by a P4R operation be situated in a strategic context in the country concerned? How would the expenditure program be framed and addressed? How would results be defined and measured to ensure the desired developmental impact? And how would disbursement be linked to achievement of results and improvement in performance? These questions are addressed in this section. (See Annex B for additional details.)

1. Strategic Relevance and Technical Soundness

30. The Bank's appraisal process would begin with an assessment of the strategic relevance and technical and institutional quality of the country's program in the area proposed for support.

(a) ***Strategic relevance.*** The Bank would seek to determine that there is a clear rationale for government intervention, that the program would address an important goal in the sector, and that performance would improve in a meaningful way.

(b) ***Technical soundness.*** The Bank would seek to ensure that the approach proposed by the government would need to be consistent with lessons and evidence from experience in the country and abroad, and would need to address key incentives that influence program performance.

(c) ***Institutional arrangements.*** The Bank would assess the adequacy of client commitment and capacity, including the capacity of key systems, for the proposed operation. The risks identified by the Bank would inform the overall risk assessment framework and the planned implementation support and other measures to address risks.

31. ***Coverage of Operation.*** While the appraisal of P4R operations would address issues similar to those addressed in IL operations, it would need to be adapted to cover the full program or subprogram to be supported. P4R operations would therefore present a valuable opportunity for the Bank to enhance its efforts to mainstream governance and accountability issues (including demand-side aspects of governance) in operational work, including by strengthening work and collaboration among sector units within the Bank and partnerships with client agencies.

32. ***Regular Reviews as Part of Implementation Support.*** A key focus of implementation support for P4R operations would be on continuing the sector/program dialogue to ensure that the elements of the program remain technically sound and strategically relevant and that any needed changes take place in a timely manner. Bank staff would also focus their efforts on institutional strengthening and capacity building to help ensure the successful implementation and longer-term sustainability of such programs.

2. Expenditure Framework

33. Linking financing to results rather than inputs requires moving beyond traditional costing exercises (which focus on inputs) to an assessment of the level, efficiency, and effectiveness of the government expenditure program to be supported by the Bank. The focus would be on a program (however broadly or narrowly defined) and not just on the share or components "financed" by the Bank. The scope of expenditure analysis would be determined by the size and complexity of the government program, and not the size of the Bank's financing. If, for example, the Bank is to support a whole sector program or a large flagship program, it would seek to ensure that the program expenditures are part of a medium-term expenditure profile that the Bank judges to be satisfactory. This would include ensuring that the budget adequately reflects the resources required to generate the expected results. It would also involve ensuring that the medium-term budget is sustainable in the context of the country's macroeconomic situation, especially the fiscal situation, and priorities for public expenditures.

34. ***Economy and Efficiency.*** The shift of Bank financing from individual transactions to broad expenditure programs would require adapting current practices to meet the "economy and efficiency" requirement of the Articles of Agreement. This would be done by evaluating government expenditures to determine that the most efficient production systems are being used and that the "pricing" of what is financed is economically sound. In some cases this may involve establishing a monetary value per unit of output (for example, the minimum cost per beneficiary required to provide a basic package of health or education services to poor households or to encourage an increase in water connections). In other cases, where it is not possible to express results in a "per-unit" form, the Bank may need to assess the overall cost of the government program relative to the proposed results, using appropriate benchmarks. Procurable items would be covered by a procurement assessment, but the economy and efficiency requirement for P4R would also be addressed for overall program non-procurable items, which will often account for the major share of expenditures under P4R operations.

35. ***Regular Reviews as Part of Implementation Support.*** Whatever specific approach is pursued, program expenditures would be reviewed throughout implementation to ensure continuing alignment with program objectives and that adequate systems are in place, while maintaining flexibility to respond to changes in circumstances. This would also provide an opportunity to review the efficiency and equity gains from expenditures, as well as their sustainability, including how well the economic assessment of the program predicted actual prices.

3. Results Framework

36. While the Bank gives attention to results in all operations, P4R operations would represent a major development by making results the basis for disbursements, and for the first

time formally codifying the link between the two. Measuring results would move from being simply one element of project design to being the primary driver of implementation. P4R operations would therefore have strong built-in incentives for both the client and the Bank to focus attention on the definition, achievement, and measurement of results.

37. ***Framework for Results.*** The Bank would appraise the results framework that defines program outputs, intermediate outcomes, program outcomes, and goals, as well as the institutional arrangements for monitoring and evaluation (M&E). With P4R operations, the focus would be on the results of the full program being supported, rather than on the results of specific activities financed by (or deemed to be financed by) the Bank. The results of the government program would be the results of the P4R. The review of previously approved P4R-type operations provides some useful illustrative examples of what results could be supported by P4R operations for various sectors and of various levels of indicators:

- Percent of women receiving antenatal care or reduction in under-five mortality (health)
- Time to start a business (private sector development)
- Percent of municipalities with paved access (transport)
- Share of public schools with active management committees (education; governance)
- Implementation of an improved system for managing procurement (public sector management)

38. ***Assessment of Monitoring and Evaluation Arrangements.*** An essential element of the appraisal of a P4R operation would be ensuring that a credible and functioning M&E system is in place. Linking disbursements to performance provides a strong incentive for a client to have a good M&E system and the capacity to implement it. In most cases, it is likely that existing M&E systems can be improved and capacity can be strengthened. Actions identified in this regard would be included in an action plan and monitored and supported during implementation.

4. Disbursements

39. ***Disbursement-linked Indicators.*** P4R operations would include a set of "disbursement-linked indicators" (DLIs)—the indicators that would be the basis for disbursements. (The term, *disbursement-linked indicators*, has been used in many existing IL projects that have P4R features.) While DLIs could vary in nature, they would be driven by desired outputs or outcomes (e.g. the number of service connections of a particular specification or number of children vaccinated or confirmed as going to school). Moreover, while it is also desirable for DLIs to be primarily outputs, they can also be complemented by intermediate outputs or process indicators (e.g. confirmation of substantive participation in decision-making by specified communities), financing indicators (e.g. share of strategic projects in total expenditures). DLIs can also be key actions aiming to address specific risks or constraints to achieving the results (e.g. implementation of an information system). It is important that the indicators are critical to achieving the outputs and outcomes efficiently and effectively. The labels do not matter as much as the key criteria—that the indicators are tangible, transparent, verifiable, and involve expenditures supported by the program.

40. The DLIs would be designed to be scalable to allow proportionate disbursement in the case of partial performance. Some existing operations already allow for the proportion of program expenditures financed by the Bank to be increased if certain targets are met or exceeded, while others provide for lower disbursement amounts when results are only partially achieved. In most cases, disbursements would be made annually or semiannually, and would be closely linked to the government's overall budgetary systems and timetables. There may be a need, in some cases, to provide advance funds to enable a government to achieve the initial DLIs. Provisions would be made for advances to be disbursed prior to the achievement of DLIs. Disbursements under subsequently achieved DLIs would be reduced by a percentage of the amount due to be disbursed under that DLI to recover part of the advance. Any advances not recovered from achieved DLIs by the closing date of the financing would be refunded to the Bank. In addition, there may be some circumstances where disbursement could be made against specific results achieved before loan approval.

41. ***Disbursement Arrangements.*** Disbursements would be made to an account of the borrower that would form part of the financial management system assessed by Bank staff. Disbursements would finance a portion of the total expenditures of the program. In most of the operations of this nature approved to date, Bank disbursements account for a modest proportion of the program;[9] however, the precise proportion is determined on a case-by-case basis. Whatever the proportion, the Bank would review the systems that apply to all program expenditures, as described in the following sections. While Bank disbursements would not be traceable to individual transactions, they would finance a defined expenditure program that is subject to the assessed accountability systems and to covenanted audit reviews. The audit scope and methodology of each operation would be customized to the circumstances of the program concerned, including, as appropriate, fiduciary, environment, social, and technical issues.

42. ***Regular Reviews as Part of Implementation Support***. Reporting on results would be a critical element of the implementation support for P4R operations. There are two dimensions to monitoring results: (a) regular M&E reporting to ensure good progress is made along the results chain as well as with respect to implementation of the agreed action plan to strengthen and enhance institutions and systems, and (b) monitoring and verification of the DLIs. P4R programs would have credible results monitoring systems including, where appropriate, independent third-party reviews, greater beneficiary participation, and civil society oversight (see Integrated Audit section in Annex B). Such measures would also help broader efforts to enhance governance and accountability at the country level by focusing on results and institutional issues as well as on the incentives for achieving desired results.

B. Systems Assessment of Fiduciary and Environmental and Social Issues

43. This section discusses fiduciary and environmental and social aspects of P4Rs, including fraud and corruption. It begins with a review of the overall approach to be adopted on these issues, and then discusses how this approach would be applied in each specific area. (See Annex B for additional details.)

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[9] A review of existing projects indicates that on average the proportion of Bank financing is usually less than 10 percent.

1. Overall Approach

44. P4R would seek to make sure that funds are used appropriately, and that the physical environment and affected peoples are adequately protected. The principles on which this would be based would be similar to those that apply to IL. However, reflecting P4R's stronger focus on results and institutional performance, the detailed procedures would be different and would apply to the entire program being supported. The new OP/BP for P4R would clearly set out these policies and procedures.

45. ***Assessments.*** During the preparation of a P4R operation, Bank staff would assess the financial management, procurement, and environmental and social impacts management systems of the implementing entities. The aim would be to determine the overall adequacy of program processes and capacity and the extent and nature of necessary improvements that would form the basis for an agreed action plan. The assessments would codify and build on the extensive experience acquired in carrying out such assessments for IL projects and through country diagnostics, and on previous experience with operations that are programmatic and have a result focus. They would also build on analytic work and lessons learned from DPL operations. The assessments would include the following: (a) a review of applicable rules and procedures and of the capacity of the implementing agencies to follow those rules and procedures, and measures that could be introduced to strengthen that capacity; (b) an assessment of the agencies' performance in implementing these procedures under the program; (c) review of the oversight mechanisms in place and measures that could be introduced to strengthen them; and (d) an overall assessment of the fiduciary and environmental and social risks and ways to manage and mitigate them. The assessments would establish, as appropriate, an initial baseline that could be monitored throughout project implementation. The documentation submitted to the Board for each P4R operation would describe the program systems, summarize the Bank's assessment of them, highlight areas where improvements are necessary, articulate the measures or the program design features agreed with the client in response to weaknesses, and identify key risks and related mitigation measures that would be taken. All the assessments would be closely coordinated and, where possible, integrated.

46. ***Use of Assessments.*** If the up-front assessments conclude that the program systems are adequate, that the implementing agencies have the capacity and the governance arrangements to implement them, and that performance is satisfactory, program preparation would proceed toward approval, and the focus of Bank staff would move to implementation support. If the assessments reveal material weaknesses, depending on the severity of those weaknesses, a decision would be made either to rule out P4R or agree with the client on measures to address and rectify them during implementation—for example, in one or more of the following ways:

(a) Where the weaknesses are so severe that credible remedial measures at the program level are judged unlikely to work, the Bank may decide not to finance the operation or, if the risks can be better mitigated by another lending instrument, to use that instrument.

(b) Measures could be identified to improve capacity, systems, and procedures, and could be supported by the Bank loan, trust funds, or another donor, or from the client's own resources. Progress in implementing these measures would be monitored during implementation. Some would be in the form of legal covenants.

(c) In certain cases, the DLIs may include specific actions, including fiduciary and environmental and social matters, as results that would be monitored during implementation.

(d) Specific actions could be agreed for inclusion in an operations manual for the program or in the internal regulations of the client, all of which would be monitored during implementation.

(e) Adjustments could be made to the terms of reference of the integrated audits and/or Bank monitoring during implementation to focus on the areas of weakness or riskiness.

47. ***Action Plans, Integrated Audits, and Implementation Support.*** As indicated above, the technical and systems assessments (including the assessment of M&E capacity) may identify concrete actions needed to enhance the system or for managing/mitigating risks. These actions would be included in an action plan for the program that would be agreed with the client and monitored as part of implementation support. Actions that are critical to achieving the outputs or outcomes of the program could be linked to disbursement and become DLIs. During program implementation, Bank staff would monitor program implementation and the performance of the systems assessed. They would also monitor progress in implementing agreed risk mitigation and performance-enhancing measures, focusing on capacity building. Integrated audits would be used, as appropriate, with the scope and frequency of such audits determined on the basis of the assessed risk. Integrated audits would focus on one or more of the following: (a) achievement of results and compliance with agreed procedures and legal covenants; (b) reasonableness of quality, cost, and other dimensions of performance; and (c) progress in implementing action plans. These audits could cross-reference findings with information generated by the regular performance assessments and drill down in areas where performance issues are identified. Implementation support would contribute to identifying areas that need strengthening with a view to improving the overall governance environment. This, in turn, would contribute to more effective implementation of the government program.

2. Financial Management

48. ***FM Assessment.*** The FM assessment, to be conducted as part of P4R preparation, would build on the extensive experience acquired in carrying out assessments of FM arrangements for IL projects, in conducting Country Financial Accountability Assessments, and in using tools developed with partners, such as the Public Expenditure and Financial Accountability reviews. The assessment would focus on the capacity and ability of the entity’s budgeting, accounting, internal controls, funds flow, financial reporting, and auditing arrangements to (a) adequately budget for all activities to be supported by the program; (b) correctly and completely record all transactions and balances relating to the program; (c) facilitate the preparation of regular, timely, and reliable financial statements; (d) safeguard assets; and (e) be subject to acceptable auditing arrangements. The assessment would focus on a clearly defined program of expenditures related to the results indicators used as disbursement triggers and would cover all sector/program funds, regardless of their source or managing institution. The assessment would focus on actual performance in addition to the formal rules and procedures.

49. ***Use of Assessment.*** The objective of the assessment would be to determine whether the entity or entities that would execute program expenditures have acceptable FM arrangements. Agreement would be reached, where necessary, on enhancements or additional controls that might be needed to ensure that the FM systems are able to adequately support any specific accounting, reporting, auditing, and funds flow arrangements required for the operation. These enhancements or controls would be included in the action plan. Approaches to strengthening the FM systems and addressing weaknesses may include support through ongoing PFM reform initiatives as well as technical and financial support as part of the operation.

50. ***Implementation Support.*** During project implementation, Bank staff would monitor the performance of the system assessed. They would also monitor progress on implementing agreed risk mitigation measures in the action plan, and review financial reports (and audits of them) that confirm whether agreed expenditures, at the appropriate level of aggregation, had been financed by the loan proceeds. If performance is lagging, the Bank would ask the client to take timely and appropriate action; and if performance continues lagging, the Bank would have the right to apply the relevant remedies.

3. Procurement

51. ***Procurement Assessment.*** In the procurement area, the Bank's assessment of the program would be based on the same key principles that are embedded in IL procurement policies, namely economy and efficiency, competition, and transparency. These principles are traditionally associated with the concept of achieving value for money in public procurement. However, such principles would be applied differently to take into account the nature of P4R operations. The Bank would assess the formal arrangements for procurement, actual procurement performance, and the procurement-related risks. The assessment of procurement arrangements would address (a) the quality of procurement procedures and whether they are based on clear, mandatory, and enforceable rules; (b) the efficiency of existing planning processes; (c) the effectiveness of external and internal controls; (d) the adequacy of staffing; (e) the integrity of the procurement process; and (f) the adequacy and capacity of contract administration. The assessment of the program's procurement performance would focus on compliance with applicable rules and take into account past performance, where feasible. It would also focus on how application of the arrangements contributes to achieving the procurement principles and supports the program's objectives and outputs by ensuring reasonable value for money. It would use data from management information systems and performance audits to assess the efficiency of procurement (in terms of timeliness, openness, cost-effectiveness, and compliance with applicable rules); the competiveness, transparency, and efficiency of the contract planning and award system; and the level of competition and whether prices paid by the implementing agency are reasonable.

52. ***Use of Assessment.*** The assessment would be used to determine whether the procurement arrangements for the program are acceptable and related risk is reasonably mitigated. The assessment would be a key input into the decision on whether the program is appropriate for P4R, including with respect to transparency, accountability, and participation. Where weaknesses are identified, the assessment may identify actions for inclusion in the action plan and/or as possible additional DLIs for the P4R operation. The Bank may support

implementation of the identified actions through technical assistance. The assessment would also be used to develop a baseline to help monitor procurement performance during implementation.

53. ***Implementation Support.*** During implementation, Bank staff would monitor procurement performance under the program and progress in implementing agreed risk mitigation measures. Bank staff would support the client in further enhancing program performance, according to institutional strengthening activities agreed during preparation. If agreements reached during the preparation of the operation are not being met or procurement performance is lagging, the Bank would ask the borrower to take timely and appropriate action; and if performance continues lagging, the Bank would have the right to apply the relevant remedies.

4. Fraud and Corruption

54. As part of the integrated assessment work outlined earlier, arrangements for dealing with risks of fraud and corruption would be reviewed. The Bank's standard remedies under the General Conditions would provide sufficient scope for the Bank to respond when issues of fraud and corruption are not being satisfactorily addressed. Moreover, the Anti Corruption Guidelines would be reviewed and modified, as needed, to ensure that they are appropriate for P4R type operations.

55. ***Dealing with Corruption Cases.*** When allegations of possible fraud and corruption are brought to the attention of the government or INT/the Bank, generally all partners should be informed and consulted. The Bank would retain the right to launch an investigation of an allegation of possible fraud and corruption under a program supported by a P4R operation. However, the preferred approach would be for government systems to carry out the initial investigation in accordance with the overall P4R approach of using and strengthening overall governance and systems. The findings by the responsible investigative unit and proposed actions would be shared with all partners and, as appropriate, the parties could consult on what further actions are warranted, including the launch of a Bank investigation. However, there could be situations (e.g. the nature of the case, lack of action or the capacity of the government) when the Bank would also conduct the initial investigations and, as needed, invoke remedies: cancellation of the loan, repayment of monies already provided, and so forth. It would also be agreed that entities that are on the Bank's debarment list would not be allowed to participate in P4R-supported programs during their periods of debarment.

5. Environmental and Social Issues

56. ***Assessment.*** The Bank would assess the system for managing and mitigating the environmental and social impacts and risks of the overall program. The assessment would be based on the following key principles:

- Avoiding or minimizing potential impacts and risk of program activities for the socioeconomic, physical, and biological environment, with due consideration to vulnerable groups including, but not necessarily limited to, indigenous peoples;
- Avoiding or minimizing involuntary resettlement and assisting displaced people in improving or restoring their livelihoods to pre-displacement levels;

- Conservation, maintenance, and rehabilitation of natural habitats and their functions or the support of efforts to realize the potential of forests to reduce poverty in a sustainable manner by integrating forests into sustainable economic development; and
- Protection of the physical cultural resources of archaeological, paleontological, religious, aesthetic or historic value.

57. The assessment approach, however, would be different than IL and would build on the existing methodology.[10] More specifically, the assessment would review the legal and regulatory framework of the systems that address environmental and social risks in the program, examining how the systems are implemented, including whether they are used to inform decisions. It would emphasize problem avoidance over mitigation, and equitable and fair treatment of affected people. It would promote transparency, information disclosure, and accountability to stakeholders, and would facilitate stakeholder consultations and participation processes. Finally, it would seek to ensure that the system has multilevel grievance redress mechanisms with specific attention to access for the vulnerable to grievance redress, and mechanisms to monitor and supervise actions on the ground that are responsive to poor performance.

58. ***Use of Assessment.*** The assessment would allow the Bank to evaluate gaps and shortcomings in order to develop institutional strengthening and capacity building activities to manage risks, mitigate adverse impacts, and enhance opportunities as part of the P4R. Specified mitigation measures would be commensurate with the potential severity of risk. The assessment of risks and related mitigation measures would feed into the operation’s overall risk assessment framework as well as the action plan. The range and complexity of potential environmental and social risks and impacts and the measures to be used to manage and mitigate them would be clearly identified, as well as the agreed steps to enhance the overall environmental and social performance and sustainability of the program. Relevant information on environmental and social issues would be disclosed by government and in an enhanced PID for P4R.

59. ***Implementation Support.*** Implementation support would involve continuous Bank engagement in monitoring and supporting the measures necessary to both ensure the soundness and enhance the environmental and social dimensions of the program. It would include following up on the agreed action plan, on the results of independent integrated audits, and on how well the grievance processes are working. During implementation, the client and the Bank would each be obliged to bring to the attention of the other party any instance of non-adherence to key principles concerning environmental and social aspects of the program and agreements reached during preparation. Clients would be obligated to take “timely and appropriate” follow-up action. If the Bank is not satisfied with progress, it would request consultations on further actions that should be taken to resolve outstanding issues in a timely manner; and if progress continues to lag, it would have the right to apply the relevant remedies.

C. Risk Assessment and Management Review

60. At different points in the operation’s cycle, the Bank—with government inputs—would undertake a risk assessment to manage the major risks to the program’s achieving its stated

[10] OP 4.00, *Piloting the Use of Borrower Systems to Address Environmental and Social Safeguard Issues in Bank-Supported Projects.*

results including (a) identifying the risks that could be avoided, those that could be managed, and those that could be mitigated; and (b) determining appropriate mitigation measures; and (c) monitoring the evolution of risks and the progress of mitigation measures and their impact. The risk assessment framework would help the government and the Bank manage in a systematic, holistic, and integrated fashion the risks that the program may not to achieve the expected results over the implementation period of the P4R operation. The framework would be used from preparation through implementation.

61. ***Risk Categories.*** The risk framework would draw on the lessons of the operational risk assessment framework recently adopted for investment lending, adapted to the program nature of the intervention. It would include the following major risk categories, at the program level:

- ***Program-related risks***, including technical soundness, financing and economic risks; fiduciary, environmental, and social risks; and performance risks.
- ***Institutional risks***, including institutional arrangements, capacity, and governance risks.
- ***Country-level risks***, including the country's politics and governance, societal and security issues, and economic management.
- ***Stakeholders' risks***, including direct and indirect stakeholders.

62. ***Use of the Assessment.*** The risk assessment, the associated risk mitigation measures, and the overall program risk rating would guide the level of management oversight. If the overall program risk is deemed to be high, Management may decide not to move ahead with preparation of the operation; or the decision to go ahead or not could be raised to the corporate level. The risks associated with the operation would be monitored not only during the preparation phase but also during implementation. In addition, in an initial phase, it is proposed to have all P4R operations subjected to an enhanced corporate oversight, involving a dedicated team (including representatives from procurement, financial management, environment and social development, and so forth).

63. ***Result, Risks, and Scope.*** The broader the scope of the program and the more ambitious the objectives for system-strengthening (e.g., with respect to fiduciary issues and social and environmental impacts), the greater the anticipated results—and the greater the risk to achievement of the projected results. Working with country counterparts, the Bank would need to come to an appropriate balance between results and risk. This may include adjustments to the scope of the program, agreement on strengthening measures to be implemented, or agreement on other special risk mitigation measures. In this context, the possible introduction of a large number of special risk mitigation measures would likely signal that the scope of the operation is too ambitious or that, given the riskiness of the environment, P4R is not the most appropriate instrument, even if the country is requesting programmatic support.

64. ***Overall Judgment.*** In reaching a final judgment on these matters, the Bank would need to be realistic and pragmatic in its assessment of the acceptability or adequacy of government systems when considering whether to use the P4R instrument to support a government program, with respect to the scope of the program, the benchmarks used to assess technical and institutional quality, and the associated risks.

D. Role of Corporate Oversight Units

65. Although P4R focuses on systems rather than transactions, it would be subject to the same oversight functions as other lending instruments. The independent corporate oversight units—Inspection Panel (IPN), Institutional Integrity (INT), the Internal Audit Department (IAD), and the Independent Evaluation Group (IEG)—would oversee P4R operations.

E. Remedies and Recourse

66. The Bank's standard remedial legal framework would apply to P4R operations. Remedies, to be distinguished from not disbursing Bank funds when DLIs are not met, could be invoked by the Bank when standard events (set out in the Bank's General and Standard Conditions) and operation-specific events (set out in the legal agreements) occur. During preparation of a P4R operation, the government and the Bank would agree on specific principles and standards to be adhered to by the client and on any actions that are deemed critical. These operation-specific undertakings would be reflected in the legal agreements and, if violated, would trigger the Bank's remedial rights. During project implementation, the Bank would monitor the government's compliance with the legal undertakings. If the systems assessed during preparation fail to perform as assessed during implementation and as mandated by the legal undertakings, and performance within the program is judged to be unsatisfactory, the Bank would require the client to institute timely and appropriate corrective measures. If such measures are not taken, posing risks to the achievement of program objectives or the appropriate use of funds, remedies would be exercised to address the situation, reflecting varying degrees of severity in the borrower's noncompliance. Remedies could include suspension of disbursement and cancellation of the loan.[11] However, the exercise of remedies in policy, procedure, and practice is normally carried out through a consultative process, taking into consideration client responsiveness and the nature of the breach.

F. New Operational Policy

67. ***Single Operational Policy and Bank Procedure Statement.*** Once approved by the Board, the P4R instrument would be governed by a single dedicated Operational Policy (OP) and Bank Procedure (BP) statement, accompanied by additional technical guidance notes or guidelines to staff.

68. ***Scope of OP and BP.*** The OP would set out the essential components of the new instrument, describing the general purposes of a P4R operation and covering the regulatory, governance, institutional, financial management, procurement, environment, and social areas. The OP would make clear that these policies apply to the entire program to be supported by a P4R operation. The BP would spell out the related procedures that would need to be carried out during preparation, appraisal, and implementation.

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[11] Section 7.02 (a) through (m) of IBRD's General Conditions and Section 6.02 (a) through (m) of IDA's General Conditions set out the events that may lead to suspension: payment failure, performance failure, fraud and corruption, cross suspension, extraordinary situation, event prior to effectiveness, misrepresentation, co-financing, assignment of obligations; disposition of assets, membership, condition of borrower or Program Implementing Entity, ineligibility, and additional event. Similar provisions are set out in Article IV of the Standard Conditions.

69. ***Guidance Notes.*** Guidance notes may discuss such technical matters as (a) how to monitor a P4R operation in general, and in relation to specific areas such as fiduciary and environment and social impacts and risks; (b) how to assess, mitigate, and monitor risks; (c) how to design and measure results and what to do if results targets are not met; and (d) how to deal with failures to comply with legal undertakings.

70. ***Conformity with Articles of Agreement.*** The Articles of Agreement contain no constraint to the proposed P4R instrument as contemplated in this concept note. The Articles provide that Bank loans should be used for productive purposes, for specific projects (except in exceptional circumstances), for intended purposes with due attention to considerations of economy and efficiency, and for expenses as they are actually incurred. Programs proposed to be financed by P4R would meet these requirements. With Board approval of the instrument, the Articles provide sufficient legal basis to allow P4R.

VII. CHALLENGES AND RISKS

71. Management believes that this proposal responds to client demand and that it will strengthen the Bank's contribution to results. But the proposal faces a range of challenges and risks, which this section discusses, together with an explanation of how they would be addressed. In some cases, these will lead either the government or the Bank to conclude that P4R is not the appropriate instrument to be used.

72. ***Specification, Verification, and Achievement of Results.*** Making results the basis for disbursements will be challenging in a number of respects. First, specifying the outcomes and outputs that the program is intended to achieve, determining the associated performance measures, and, where relevant, mapping intermediate results/indicators to final outcomes is a complex challenge. Second, with Bank financing conditional on measured results, there may be pressures on both clients and Bank staff to compromise on results measurement. Third, to the extent that expected results are not achieved and disbursements cannot be made, some clients may face financing gaps in important development programs and challenges in filling those gaps.

73. To address these challenges and risks, it would be essential to develop adequate quality assurance and guidance mechanisms. The Bank would support capacity to develop sound results frameworks and to monitor and evaluate such frameworks, not only for clients, but also for Bank staff, including through training. P4R operations would seek to establish independent verification and monitoring mechanisms, with transparent, timely, and accurate reporting and clear requirements for follow-up actions if problems are identified. Making DLIs scalable, to allow for proportionate disbursement in the case of partial achievement of results, would also help reduce the financing risks for governments. A separate guidance note on how to develop and implement results frameworks for P4R operations will be prepared, building on the outline provided in Annex B.

74. ***Adequacy of Fiduciary and Environmental and Social Impact and Risk Management Measures.*** P4R operations would provide assurance that Bank financing is used appropriately and that the environmental and social impacts and risks of the program are satisfactorily addressed. This assurance would be heavily influenced by the adequacy of the systems being supported, plans to improve the systems, and the risk mitigation measures that will be adopted as a complement to expected system improvements. While such an approach has the potential to

achieve even greater development impact than a more transactions-based approach, it also runs the risk of being perceived as a lowering of Bank standards.

75. To address this risk, assessments would be carried out rigorously, consistently, and transparently; the measures to improve existing systems would be meaningful and realistic; and the agreed risk mitigation measures would be appropriate to the circumstances. Guidance would be provided to staff and enhanced internal review mechanisms would be put in place. In addition, the P4R consultation and communications plans would pay particular attention to these issues.

76. ***Effectiveness of System Strengthening and Capacity Building.*** Institutional strengthening and capacity building to ensure that programs achieve their expected results is a core feature of P4R, especially in situations of weak capacity. But institutional and capacity building are challenging. Some countries may be unwilling to request Bank financing for the technical assistance and other measures necessary to help build capacity.

77. To address this challenge, Bank implementation support activities would focus on capacity building in a broad range of areas, including the program's results frameworks and its fiduciary and safeguards systems, processes, and procedures. The Bank would support institutional strengthening and capacity building as a core element of P4R operations, and, as needed, through complementary analytic work and technical assistance. It would also develop partnership arrangements with other development partners, which may be in a better position to support the necessary capacity building, including through grant finance in certain countries.

78. ***Risk of Results or Other Actions Being Imposed on Countries.*** P4R operations provide a major opportunity to improve development partner coordination around government-owned programs, thereby contributing to significant improvements in both the efficiency and effectiveness of development assistance. But in countries where there are many development partners and development assistance accounts for a very large proportion of the financing of a government program, there is also the risk of development partners (perhaps inadvertently) imposing results on countries and programs or insisting on the use of external review mechanisms of various kinds, thereby contributing to new forms of conditionality.

79. Governments and development partners all need to be aware of and guard against such risks. While vigorous debate should be welcome and rigorous review is essential, the success of P4R operations depends crucially on the programs' being government-owned and government-led. As the likely lead donor for many of these programs, the Bank would have a particularly important role to play in ensuring meaningful government ownership and leadership of the programs to be supported through P4R operations.

80. ***Use of P4R.*** The various assessments that are integral to the P4R instrument would need to preserve the flexibility necessary to ensure that the instrument is available to a broad range of countries and sectors.

81. The Bank would need to find the right balance between preserving the flexibility of the instrument and ensuring that it is used only in contexts where it can be expected to achieve the desired results.

82. ***Readiness for Introduction of the Instrument.*** In view of the clear demand for the new instrument, there is some urgency to proceed with its further development and introduction. But it is also clear that the introduction of such an instrument would add to the Bank's menu of lending instruments, and Management and the Board need to ensure that the instrument is ready to be introduced.

83. While the P4R would be a new instrument, there is broad experience with using P4R-type features in IL operations in recent years. In many ways, the introduction of the P4R would codify the lessons learned from that experience. In addition, it would be important that the consultation process reflect the significance of the proposed change. Taking account of the results of the consultation process, detailed guidelines to staff would need to be prepared to accompany a new OP/BP. Management would also put in place enhanced oversight (see para. 90 below) to ensure effective use of the new instrument. The new policy and associated guidelines and the proposed oversight arrangements would be discussed with the Board before the approval and introduction of the new instrument.

84. ***Risks of "Muddling Along".*** There are important challenges and risks that need to be addressed in the further development and implementation of the P4R instrument. But there are also major risks in not developing such an instrument. As this paper has described, the current "muddle-through" approach is resulting in inconsistent and selective application of programmatic approaches across the institution, with missed development opportunities, and significant frustrations to borrowers and Bank staff. It also seems clear that including P4R under the current menu of IL options[12] and existing IL fiduciary and safeguard policies would likely result in P4R getting caught up between the transaction-orientation and the systems focus, a risk that would make the tool of limited value to many client countries.

VIII. NEXT STEPS

85. If strong demand, support of key stakeholders, and alignment with institutional goals and objectives are key ingredients for the success of a reform program, then the proposed P4R instrument has a strong potential for success. If the concept and approach are endorsed, the key next steps would be as follows.

86. ***Consultation with Stakeholders and Shareholders.*** This concept note would form the basis of broad internal and external consultation (with Bank staff, the Board, client countries, partners, donors, other multilateral development banks, and civil society organizations). These global consultations—web-based and face-to-face—would include IDA and IBRD borrowers, fragile states, and countries with large and small operations. A dedicated webpage would host the range of consultation materials in six languages: Arabic, Chinese, English, French, Russian, and Spanish. The consultation plan would be publicly available on the Bank's external website and would outline areas in which feedback will be sought. A set of guiding questions would provide the framework for the discussions/feedback—that is, the overall concept and approach of P4R, its potential for development effectiveness and capacity building, its risks, and fiduciary and

[12] The current menu of seven IL options include: Adaptable program loan (APL), emergency recovery loan (ERL), financial intermediary loan (FIL), learning and innovation loan (LIL), specific investment loan (SIL), sector investment and maintenance loan (SIM), and technical assistance loan (TAL).

environmental and social issues. Detailed information about the consultations—participant lists, discussion summaries, and so on—would be publicly available on the consultation webpage. An overall summary of the consultations would be compiled and a summary included as a supporting document to the final paper.

87. ***Preparation of Supporting Documents.*** Reflecting the feedback from the consultations, the Bank would prepare the necessary documents to support the introduction of the new lending instrument (OP/BP documents, any amendments that may be needed to legal documentation, and guidance and training materials for staff) and any changes that may be needed to the internal information systems. With respect to the assessments required of the program as a whole as well as the fiduciary and environmental and social dimensions, a sizable amount of material is already available, but further work is still required. A paper setting out the full details of the new instrument would be brought to the Board for discussion and approval by the end of FY11.

88. ***Staff Guidance.*** Staff would be provided with substantial guidance and support in implementation. Management would work to balance consistency in policy application (and in particular to address potentially inconsistent interpretations from within individual departments) with the need to adapt to diverse client situations and to innovate. Training would be included in the core curriculum for task teams that is currently under construction. Communications and additional training and orientation would be carried out in consultation with the Regions.

89. ***Communications and Outreach.*** In addition to staff guidance and training, the introduction of the new instrument would be supported by a comprehensive internal and external communications and outreach effort.

90. ***Enhanced Oversight and Stocktaking.*** In the initial phase, enhanced corporate oversight would be put in place to ensure the appropriate and consistent application of the new lending instrument. This builds on the experience of introducing other new initiatives, such as Additional Financing. The proposed corporate oversight would involve a dedicated team (including representatives from procurement, financial management, environment and social specialist, and so forth) to review all new P4R operations. In addition, Management would develop a plan to review implementation experience and to adapt either the instrument or its use as appropriate. Management would prepare a review of implementation for discussion with the Board after an agreed period or lending volume, to be decided.

91. ***External Consultations.*** Following Board discussion, Management will proceed with external consultation on the basis of this Concept Note. In soliciting comments from a wide variety of stakeholders, the Bank would ask them to consider questions such as the following:

(a) The Bank is planning to introduce a new lending instrument with its own operational policy to finance government programs and disburse against results. Would you support the introduction of an instrument to support investments at a program level (as opposed to project or overall budget support)? Do you support linking the disbursement to results?

(b) The proposal for P4R calls for supporting a spectrum of results, depending on the nature of the program, and for making the instrument open to all countries and sectors, subject to their meeting the appraisal criteria. Do you agree/disagree with the flexibility in the definition of eligible results? Do you agree/disagree with the openness of the instrument to all countries and sectors? Please explain, as needed.

(c) P4R proposes to address fiduciary issues at the program level instead of a transactions level. This will imply that the assessment work and supervision will also be carried out at the program level. The proposal highlights one benefit from the approach—improving the performance of the overall program instead of a ring-fenced project. Do you agree with this approach?

(d) Similarly, the P4R proposes to address the management of social and environmental impacts at the program level, and appraisal would focus on reviewing existing system to manage such impacts, the performance of the system, and capacity to implement. The focus of implementation support would be on the performance of the system and the systems improvements, if warranted. Do you agree with this approach?

(e) In addition, the Bank would welcome other suggestions or comments that stakeholders and shareholders may have.

ANNEX A. SUMMARY OF EXPERIENCE

1. In October 2009, OPCIL carried out a review of the Bank's experience with various lending operations that incorporate P4R-type features (referred to here as "programmatic IL): sectorwide approaches (SWAps), conditional cash transfers (CCTs), output-based aid (OBA), results-based financing in health (RBFH), and operations under the Education for All—Fast-Track Initiative (EFA FTI). The review also looked at the approaches of three external agencies created in the last decade that are among those that pursue important dimensions of program-based aid—the Global Fund to Fight AIDS, Tuberculosis and Malaria, the Millennium Challenge Corporation (MCC), and the GAVI Alliance. This sample is intended to illustrate approaches and lessons learned as well as the demand for results-based instruments.

A. Sectorwide Approaches

2. Since the mid-1990s, an increasing number of Bank operations support sectorwide programs. A very recent analysis of the SWAp project performance identified 111 IBRD/IDA SWAps (including pre-SWAps) approved since 2000, with a combined commitment amount of $16.5bn. In terms of volume, 46 percent of SWAps are in LCR and 26 percent in AFR, but AFR has the greatest number of projects, 50. Of the 111 SWAps, the largest percentage ($ volume) were in social protection and education, and public sector governance.

3. ***Evolution of SWAps.*** SWAps are now used in environments well beyond those in which they started in the 1990s (largely social sectors in donor-intensive countries in AFR and SAR). They have grown strongly in middle-income countries, notably in LCR, where the approach has been significantly adapted in response to country conditions. They have grown beyond social sectors to include water, transport, agriculture, and others. The Regions report that client demand for SWAps is strong. SWAps have helped advance donor alignment to country strategies, better coordinate donors, and make significant institutional change and reform in many countries, notably in public financial management. The SWAp concept has been a platform for innovation and greater flexibility. It has also allowed the Bank, other donors, and the countries themselves to focus more strongly on results. A very recent analysis of SWAp project performance also shows indicators that compare favorably with the overall lending portfolio, with the share of commitments at risk and problem projects significantly lower.

4. ***Challenges.*** At the same time, there have been difficulties. Initial assumptions have often proved too optimistic, especially in terms of low-income countries' institutional capacity to manage larger and often more complex programs. The early momentum in some (mainly low-income) countries has been difficult to sustain. SWAps have increased the transaction costs for donors, particularly the lead donor. New donors, especially in the social sectors, have found the SWAp framework insufficiently flexible to allow the degree of focus they wished to have on the area to which they are dedicated. Some established donors, including the Bank, have judged it appropriate to do stand-alone, parallel interventions alongside SWAps. The absence, whether perceived or real, of clear policies and guidance on SWAps has led to confusion and inconsistent approaches among staff. Bank staff routinely report the internal processing costs of these types of operations to be excessive, diverting time and attention from substantive matters. More

recently, there has been a lack of clarity over the applicability of the Bank's fiduciary and fraud and corruption policies in an IL environment in which the Bank finances broader expenditure programs rather than individual transactions.

B. Conditional Cash Transfers

5. CCTs have grown strongly in the last 15 years.[1] The Bank estimates that they are being implemented in more than 30 countries, with the heaviest concentration in LCR, but with large-scale programs in Bangladesh, Philippines, and Turkey, and with pilot programs in Cambodia, Malawi, Morocco, Pakistan, and South Africa. In addition, there has been impressive growth in the numbers of beneficiaries reached: Mexico's PROGRESA, which started with approximately 300,000 beneficiary households in 1997, now covers 5 million households;[2] and Bolsa Família in Brazil now covers 11 million families, or around 46 million people—almost one-quarter of the population. Bank support for CCT programs has grown sharply. It is mainly concentrated in LCR, where the Bank has approved $3.8 billion in loans to support 14 operations in nine countries. The largest sectoral concentration is in social protection, followed by education. The Regions report strong demand for further CCT lending.

6. ***Results.*** CCT operations compare well to the total portfolio, and there is considerable evidence that CCTs have improved the lives of poor people. Transfers generally have been well targeted, have raised consumption levels, and have reduced poverty—by a substantial amount in some countries. CCTs have provided an entry point to reforming badly targeted subsidies and upgrading the quality of safety nets, while making sure that offsetting adjustments have been modest. CCTs also have a strong evaluation culture, well beyond traditional practice in social policy; and this culture is spreading from one CCT to another, as well as to other programs in the same country. At the same time, the evidence on improvements in final outcomes in health and education is more mixed. CCTs have worked best when the supply side has been in place to respond to the demand. This is a good example of how various Bank instruments and tools can help countries achieve optimal outcomes when applied to solving the appropriate constraint.

C. Output-based Aid

7. OBA, broadly defined, seeks to tie disbursement to the achievement of specific outputs. The Bank-administered Global Program on Output-based Aid (GPOBA) started in 2000 to both directly support OBA activities using trust funds and promote the wider use of OBA in the development community.[3] With a modest level of resources, the program used a more focused definition of OBA—a mechanism that ties the disbursement of explicit, performance-based subsidies or grants to the achievement of specified outputs that directly support improved access to basic services by poor households.[4] GPOBA has supported such basic services as improved water supply, energy, health care, education, information and communications technology, and

[1] See *Conditional Cash Transfers—Reducing Present and Future Poverty*, World Bank Development Research Group, February 2009.

[2] This program, now known as *Oportunidades*, is supported by an IBRD loan of $1.5 billion, the Bank's largest CCT loan.

[3] See www.gpoba.org and *Output Based Aid: A Compilation of Lessons Learned and Best Practice Guidance*, GPOBA/IDA-IFC Secretariat, June 2009.

[4] GPOBA also draws a distinction between OBA and output-based disbursement (OBD), defining the latter as disbursement to improve the efficiency of assets or government systems, while OBA tends to support private provision of services.

transport. It places particular emphasis on explicitly targeting output-based subsidies to the poor. Hence, an OBA subsidy finances the funding gap between the cost of service delivery and the beneficiaries' ability and willingness to pay user fees for the service. Services are contracted out to a third party (service provider) through either a competitive process or a single-source selection process, in both cases following Bank Procurement Guidelines, with elaborate processes in place to determine the amount of subsidy, share risk, and independently verify the output.

8. ***Results.*** The OBA portfolio includes 115 closed and active projects. Of these, 57 projects are funded by IDA, 25 by IBRD; and the remaining projects by trust funds and GEF. The size of the OBA subsidy portfolio is at $4 billion. With $2.5 billion, IBRD has the largest share of the OBA subsidy portfolio despite the smaller number of projects. Most of the projects are in AFR (because of recent piloting efforts by GPOBA) and in LCR (where the first OBA pilots in many of the sectors reviewed began). In terms of subsidies, LCR accounts for 51 percent of the total volume, while AFR accounts for 23 percent of projects that are active or have closed. Disbursements have similar shares. It is estimated that of the active and closed projects with OBA components, 80 percent of the funds—$3.2 billion—have been disbursed. The largest share of OBA projects, both in terms of volume and number of projects, is under the Transportation Sector Board. Energy & Mining, Health, and Education also have relatively large shares in OBA projects.

9. ***Challenges.*** GPOBA considers that the main challenge for mainstreaming OBA approaches lies in reconciling the Bank's requirement that investment lending needs to be "expenditure-based" with the "performance-based" nature of OBA and similar mechanisms. It wishes to see the Bank go beyond the guidance is has provided to staff on procurement for OBA. Specifically, it would like to see incentives for innovation and a greater emphasis on outputs rather than inputs, including more amenable fiduciary procedures. It sees IL reform as the initiative to address these issues.

D. Results-based Financing for Health

10. In general, results-based financing mechanisms operate on the basis of payment for agreed outputs rather than the traditional payment for inputs. For several years the Bank has worked with other donors to promote results-based financing in health delivery, in which payment to a provider, payer, or consumer is made when measurable actions are taken or defined performance targets are achieved.[5] RBFH is an innovative financing strategy that aims to increase the impact of investments in health by providing a financial or in-kind reward upon achievement of agreed performance goals. It is an umbrella term that includes output-based aid, performance-based financing, provider payment incentives, vouchers, contracting linked to particular targets, and conditional cash payments and transfers to households. In some countries, RBFH may take the form of paying a bonus to health facilities that meet certain quantity or quality targets, such as percent of women delivering their babies in a facility. Other countries are designing RBFH mechanisms to provide incentives and support to poor people to overcome hidden barriers—such as the cost of transport—to using services.

[5] See www.rbfhealth.org and *Taking Stock: World Bank Experience with Results-based Financing in Health*, Brenzel and others, HDNHE, World Bank, June 2009.

11. ***Prevalence, Scope, and Support.*** A recent stocktaking of Bank RBFH experience identified 260 active and closed projects over the period FY95-FY08. Of these, 15 percent identified an RBFH element, which was considered "substantial" in 60 percent of the cases. Of those considered "substantial," 43 percent were in LCR and 27 percent in AFR. Most of these projects were approved in the last five years. The mechanisms spanned a wide range—from performance agreements with national and subnational governments, insurance entities, public facilities, private providers, and NGOs; to performance-based worker incentives and arrangements with communities; to conditional cash transfers. The dominant Bank lending instrument was IL. The total value of support by IBRD/IDA was $3.79 billion, and IDA financing represented 68 percent of support in active projects. RBFH received an added impetus in September 2009, when members of the High-Level Task Force on Innovative Health Financing committed a total of $5.3 billion to accelerate progress toward the Millennium Development Goals. The UK and Norway will contribute $420 million to support results-based financing programs and buy-downs to improve maternal and child health, and the Government of Australia will provide AUD336 million over the next four years for performance-linked aid to help partner governments in Asia and the Pacific. A significant portion of the new funds committed will be channeled through the Bank's Health Results Innovation Trust Fund. Teams working in this area have noted that the Bank is missing opportunities for adding impact through results and have identified several areas for attention: the need for feasible mechanisms for disbursing against results, for help to staff to put in place adequate monitoring frameworks (including baseline data), for better analysis, for integrating RBF into bigger operations and initiatives, and for in-country capacity building.

E. Education for All—Fast-track Initiative

12. EFA FTI was created in 2002 to help low-income countries achieve free, universal basic education by 2015.[6] Eighteen donors pledged $1.6 billion to the FTI Catalytic Fund in the period 2003 to 2010. Of this, $1.47 billion had been committed to 31 countries (all IDA) as of September 15, 2009, with 42 percent disbursed. FTI expects 25 to 30 low-income countries to apply for financial support before the end of 2010, creating a funding shortfall of US$1.2 billion, with an additional several billion US dollars required after that date to meet 2015 education goals.

13. ***EFA Compact.*** Under the EFA Compact, partner countries commit to develop sound education sector programs through broad-based consultation, show commitment to education through strong domestic support, demonstrate results on key performance indicators, and exercise leadership in developing and implementing the program and coordinating donor support. Donors commit to help mobilize resources and make them more predictable, align with country development priorities, coordinate support around one education plan, and harmonize procedures as much as possible. The initiative seeks to apply the 2005 Paris Declaration on Aid Effectiveness. Staff and partners associated with the program report that rigid application of existing Bank fiduciary rules (mainly procurement), or failure to adapt them to the programs being supported, causes unnecessary delay and undermines program implementation and the achievement of results.

[6] See www.educationfasttrack.org and *A Fast Track to 2015: Educating the World's Children for a Better Future*, October 2009.

F. Global Fund to Fight AIDS, Tuberculosis and Malaria

14. The Global Fund to Fight AIDS, Tuberculosis and Malaria is a global public/private partnership—of governments, civil society, the private sector, and affected communities—dedicated to attracting and disbursing additional resources to prevent and treat HIV/AIDS, tuberculosis, and malaria. It works in close collaboration with other bilateral and multilateral organizations. Created in 2002, the Global Fund has become the main source of finance for programs to fight the three diseases, with approved funding of US$15.6 billion for more than 572 programs in 140 countries. Globally, it provides one-quarter of all international financing for AIDS, two-thirds for tuberculosis, and three-quarters for malaria.[7]

15. ***Operating Model.*** The Global Fund placed performance-based funding at the heart of its operating model, to ensure that funding decisions are based on a transparent assessment of results against time-bound targets. This approach promotes accountability and provides incentives for recipients to use funds efficiently to achieve results. Global Fund programs receive initial funding on the basis of the quality of their applications. To receive subsequent financing, they must demonstrate results against defined performance targets. These targets are proposed by the country (for approval by the Global Fund) to ensure that they are appropriate to the national context and local program realities. This system of performance-based funding was developed to

- Link funding to the achievement of country-owned objectives and targets;
- Ensure that money is spent on delivering services for people in need;
- Provide incentives for grantees to focus on programmatic results and timely implementation;
- Encourage learning to strengthen capacities and improve program implementation;
- Invest in measurement systems and promote the use of evidence for decision-making;
- Provide a tool for grant oversight and monitoring within countries and by the Global Fund Secretariat;
- Free up committed resources from nonperforming grants for reallocation to programs where results can be achieved.

16. ***Fiduciary Procedures.*** Unlike EFA FTI, the Global Fund chose not to use Bank fiduciary procedures, which were seen as too rigid. At the same time, the Global Fund is committed to strong fiduciary performance. It received advice and assistance from the Bank in establishing its own fiduciary arrangements. Its experience well illustrates the difficulties posed by equating specific operating procedures (which can quite appropriately vary from country to country, or from organization to organization) with overall fiduciary objectives, for which there is universal support. The Bank's challenge is to avoid having the specific technical procedures it has developed (procedures that often serve as a global reference point) prevent operational collaboration with countries and partner organizations that are equally committed to the same fiduciary objectives, but that choose to reach them through somewhat different technical procedures.

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[7] See www.theglobalfund.org.

G. The Millennium Challenge Corporation

17. The MCC was created in 2002 as an independent U.S. foreign aid agency to help in the fight against global poverty in innovative ways. Rather than delivering development finance in traditional ways, it seeks to focus on good policies, country ownership, and results.[8] The MCC places great emphasis on achieving and measuring results, concentrating on identifying activities that have the greatest promise of poverty reduction through growth, measuring progress during implementation, and learning from experience.

18. ***MCC Approach*****.** The MCC has approved $6.9 billion in "compact" funding to 19 countries, and $470 million in "threshold program" funding to a further 19. It has disbursed $1.1 billion. Beneficiary countries are selected competitively on the basis of 17 policy indicators and their policy performance. The countries selected are required to identify their priorities for achieving sustainable economic growth and poverty reduction, and to develop their MCC proposals in broad consultation within their society. For compact countries, a local, country-owned Millennium Challenge Account accountable entity is set up to manage and oversee all aspects of implementation. Funding has been for in such sectors as agriculture and irrigation, transportation (roads, bridges, ports), water supply and sanitation, access to health, finance and enterprise development, anticorruption initiatives, land rights and access, and access to education.

H. The GAVI Alliance

19. The GAVI Alliance (formerly known as the Global Alliance for Vaccines and Immunization) was launched in 2000 as a global health partnership of both private and public sectors to accelerate access to underused vaccines, strengthen countries' health and immunization systems, and introduce innovative new immunization technology, including vaccines. The partnership comprises developing world and donor governments, private sector philanthropists such as the Bill & Melinda Gates Foundation, the financial community, developed and developing country vaccine manufacturers, research and technical institutes, civil society organizations, and multilateral organizations like the World Health Organization (WHO), the United Nations Children's Fund (UNICEF), and the World Bank. It aims to contribute to achievement of the Millennium Development Goal for child health—a two-thirds reduction in the number of deaths in children under five years of age by 2015.

20. ***GAVI Approach.*** GAVI support is subject to performance monitoring designed to track progress achieved in the previous year, declare planned targets for the following year, and verify the sustainability of existing financing mechanisms. It therefore gives considerable prominence to monitoring through annual progress reporting, data quality auditing, and vaccine management assessment. An Independent Review Committee reviews each annual progress report, making technical comments and suggestions, and recommends one of the following three outcomes to the GAVI Alliance Board—to continue providing support, request clarifications before continuing to provide support, or request the country to resubmit its report as insufficient information has been provided. Independent verification is pursued though data quality audits, which are required for countries receiving immunization services support during the second year.

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[8] See www.mcc.gov.

ANNEX B. TECHNICAL ASSESSMENTS

A. Introduction

1. The main text of the report provides the rationale for a new instrument, Program-for-results lending (P4R), which would complement the Bank's two existing instruments, development policy lending (DPL) and specific investment lending (SIL). As part of the appraisal process, all Bank-financed operations are assessed from a technical perspective as well as with respect to fiduciary and social and environmental concerns, in accordance with the relevant operational policies (OPs) and Bank procedures (BPs). Such assessments would also apply to P4R operations, which would be governed by a single dedicated OP/BP covering all relevant policy concerns, including fiduciary and environmental and social impacts. This annex provides some initial guidance on how these assessments would work in P4R operations. The full details will be elaborated in detailed Guidance Notes to staff and clients before the roll-out of the new instrument.

2. ***Structure of this Annex.*** The annex is organized into three main sections. Section B discusses the technical assessment, which includes examination of the strategic relevance and technical soundness of the program, the expenditure framework, and the results framework including disbursement. Section C explains how due diligence would be carried out with regard to fiduciary issues—procurement, financial management and concerns about fraud and corruption—and covers the assessment of the adequacy of systems for managing environmental and social impacts, risks, and sustainability. Section D introduces a risk assessment framework that would identify areas and levels of risk of the operation; the level of Management scrutiny that would be needed during preparation and focus implementation support on the identified risks, their management in addition to capacity building.

B. Technical Assessments

1. Strategic Relevance and Technical Soundness

3. A critical part of the Bank's appraisal process would be the assessment of the strategic relevance and technical soundness of the government program. Is the program addressing an important goal in the sector? Is there a clear rationale for government intervention? If the operation is successful, would performance be improved in a meaningful way? This assessment would typically require some element of analysis. For example, if the stated goal of the government program is to improve the quality of education, the assessment ought to provide some indication that low quality is indeed a serious problem. Or if the goal is to support an expansion in "pro-poor access" to water connections, some evidence should be provided that the country (or region) is lacking in this area.

4. This would be followed by an assessment of the technical soundness. Is the approach proposed by the government consistent with lessons and evidence from experience in the country and abroad? Would it address the key "behavioral" bottlenecks hindering the performance that the operation is seeking to improve? For example, if the problem is low access to water connections among poor households caused by high connection costs, is the program proposing a

reasonable strategy to increase effective demand for water connections? Or if the problem is low quality of education services, has the program identified the key drivers for change as they relate to availability of pedagogical inputs or teacher presence and motivation?

5. The assessment of technical soundness must be complemented by an assessment of institutional arrangements. Under IL operations, such arrangements usually focus on implementation arrangements for specific projects and the contracting of Bank-financed inputs. Since the focus of the P4R would be on supporting the government's program, the institutional assessment should focus on the program level. Are the institutional structures for implementing the program adequate? How can they be improved? Are the structures for managing and administering the program satisfactory? Do the agencies involved have the critical staffing, skills mix, and budget for implementing the program? If the program involves several agencies (as in decentralized programs), are incentives in place for adequate quality and cross-agency collaboration? Equally important, what are the institutional arrangements for monitoring and reporting on program performance and verifying inputs, expenditures, outputs, intermediate outcomes, and final outcomes? By focusing on institutional assessments at the program rather than the project level, P4R operations would provide a particular opportunity for the Bank to continue enhancing its ongoing efforts to mainstream governance and accountability issues in operational work, including by strengthening work and collaboration among sector units and partnerships with client agencies.

2. Expenditure Framework

6. This section describes the Bank's proposed approach to the appraisal of the economic and financial aspects of P4R operations. The P4R operation's equivalent of an IL project's financial analysis would be an evaluation of a medium-term (three to five years) projection of the program's budget for its consistency with the program's objectives and its feasibility and sustainability in the context of the country's overall fiscal situation. This approach to financial analysis would involve an understanding of both expenditures and their sources of financing over a specific time period. This methodology is well established and has been used over the years by Bank staff in program support and SWAps, and as part of analytic work for Public Expenditure Reviews.[1] In assessing a program's medium-term budget, the Bank would apply certain criteria. The first is that the medium-term budget adequately reflects the estimated costs of the program and its stated objectives. The medium-term budget has to be sustainable in the context of the country's macroeconomic situation, especially the overall fiscal situation, and priorities for public expenditures as set out in its recent major policy documents. If under those circumstances the Bank were appraising a proposal for a P4R involving a large program (with a sizable initial share in the overall budget) and a large projected increase in program expenditures, it would seek assurances from the government that such an expansion is indeed possible. The analysis should also examine if there has been a recent pattern of major discrepancies between budget allocations, releases, and actual expenditures. Gaps between budget allocations and releases may be indicative of a pattern of overestimation of government revenues (usually a government-wide feature, rather than specific to any given program). On the other hand, if releases have been timely and in line with the corresponding budget allocations, but actual program expenditures have fallen short of the amounts released, that would suggest that the program's implementing

[1] Public Expenditure Management Handbook, The World Bank (1998), pages 41-42.

agencies have had insufficient capacity to carry out their planned activities. The Bank would need to ascertain and assess what changes the government intends to make to enhance the implementation capacity of the relevant agencies.

7. The economic analysis would focus on the expected efficiency that would result from the successful implementation of the program to be supported by the P4R operation. The analysis would examine two key aspects of the program. First, the economic analysis would examine if there is a clear rationale for government intervention in the relevant sector or subsector, and the related question of whether that intervention should take the form of regulation, financing, or outright provision?[2] Priority is generally given to areas where a potential market failure exists and direct provision or financing of certain goods and services by the government appears to be the best intervention modality.

8. Second, the economic analysis would seek to examine the efficiency related to the program (relative to the counterfactual of continuing the program in its present form). The efficiency gains may sometimes be quantifiable, but often the discussion will be qualitative in nature. The specifics would very much depend on the nature of the relevant sector or subsector—for example, health facilities or schools that are fully staffed but have meager budgets for non-wage expenditures such as drugs and instructional materials; infrastructure investment programs that do not make sufficient allowance for maintenance; and agricultural extension programs that do not promote the most suitable production technologies for local conditions. In all these cases, meaningful reforms to be supported by a proposed P4R operation would result in efficiency gains that would not have materialized if the program had continued in a "business as usual" mode. Another set of efficiency gains would be related to the strengthening of procurement and financial management practices as part of the operation, if needed. In some cases, additional analysis would be conducted related to specific aspects of the program like equity gains and poverty reduction. For instance, the analysis could look at distribution of the program's benefits, or access to the program or services rendered. Such analysis could take into account access to the program services or benefits by specific groups—for example, (a) universal provision or access versus targeted access for the poor (distributional analysis of benefits by income groups); (b) access by specific vulnerable groups, such as ethnic minorities, the unemployed, the elderly, disabled, or youths; or (c) geographic or spatial distributional considerations (all regions of the country vs. targeted regions; urban vs. rural; etc.). The analysis may also include impacts on poverty and inequality. Finally, for certain programs, the Bank's economic analysis may extend to other dimensions, depending on the nature of the service delivery in question.

9. In addition to the more traditional public expenditure and budget analysis, it would also be important to examine the alignment of the expenditures with the key objectives and the institutional arrangements. Understanding the incentive structure for reforms or improving performance of a program is key to its success. The program expenditure analysis would provide important insights in this area.

[2] See Evaluating Public Spending: A Methodological Framework for Public Expenditure Reviews, by Sanjay Pradhan, World Bank Discussion Paper Number 323, February 1996, page 2.

3. Results Framework

10. The Bank has long recognized the importance of having clear results frameworks and plans for monitoring and evaluating in all the operations it funds, but this is often an area of weakness. P4R, by making results the trigger for disbursements, represents a fundamental change in this regard. In P4R, measuring results is not just one more aspect of the project, but a key design feature and an important driver for implementation. In other words, P4R operations have strong built-in incentives for both the client and the Bank to focus attention on measuring and achieving results.

11. The results framework defines the program outputs, intermediate outcomes, program outcomes, and goals. It is important to stress that the results of the government program would be the results of the P4R. However, where a government program has an extremely detailed set of results, the results used for the P4R could be a subset of the full program results. This would be done to ensure proper monitoring and sufficient capacity to achieve the results. Results of a P4R operation are not external conditions imposed on countries; rather the P4R operation would be an opportunity to enhance the performance of government programs by strengthening the focus on their own results and linking funds to their achievements.

(a) Assessing Monitoring and Evaluation Capacity

12. Assessing the monitoring and evaluation (M&E) capacity of the program would be an essential element of appraising the P4R operation. If weaknesses are identified, remedial measures would be developed and indicators related to strengthening M&E capacity could be included in the set of DLIs or as part of an agreed action plan. An assessment of the M&E capacity of existing systems would cover the following aspects:

- Institutional setup for monitoring and evaluating results (i.e., clear specification of key actors and institutional roles for monitoring and reporting; information needs, data sources and frequency; an assessment of capacity and a plan for developing capacity as needed).
- Existing M&E plans: what is being measured and how?
- Quality and reliability of existing M&E products: evaluations, data, information systems, progress reports.
- The framework to support effective M&E and information-sharing, (e.g., data sharing/disclosure policy, performance-based budgeting policies and regulations).
- Staffing and resources to support M&E functions.
- Capacity development needs.

(b) Defining DLIs

13. DLIs play an important role in P4Rs because they trigger disbursement of funds in support of the government program. While in principle, DLIs are either outputs or outcomes, they can also be indicators deemed critical for strengthening and enhancing performance, they can include a range of results ranging from process to intermediate outcomes that help achieve the desired outputs and outcomes. For instance, they can include measures to strengthen the

performance of program management, financial management, procurement processes, environmental and social aspects, oversight and controls, monitoring and evaluation, and so on.

14. ***Key Design Features*.** DLIs need to be considered carefully as key results that will influence the achievement of the development objectives. The DLI may also focus on a milestone that is considered critical to achieving the PDO. For instance, if the PDO of the government's program is to improve the quality of basic education, the DLIs selected could include the percentage of students taking external assessment examinations, with comparative results published and sent to all municipalities and schools. This intermediate result is an indicator of improvements in the education assessment system to measure performance and quality improvements. Alternatively, the selection of a particular DLI may relate to the importance of "signaling" and providing incentives for key institutional changes, outputs, or outcomes. Such incentive-driven DLIs can help foster a culture of performance-based management well beyond the Bank's results-based financing. For instance, the percentage of schools with gains in student performance in the fourth grade represents an actual "outcome" indicator for improved quality and performance of the education system—and could encourage the use of "incentives" for performance-based management within the government's system.

15. ***Selecting DLIs.*** When selecting and structuring DLIs, the following points should be considered:

- ***Which milestones have key influence in achieving the PDO*?** The selection of the DLI should focus on the indicators that are needed to provide evidence of continued progress toward the expected PDOs. The choice of DLIs should also be clear with respect to its signaling purpose. Does the DLI serve the role of signaling and monitoring a critical milestone along the results chain, without which the program's development objectives could not be achieved? Or does the DLI serve the role of signaling incentives for rewarding performance (outputs, outcomes), to encourage the practice of managing for results?
- ***How many DLIs?*** Not all milestones on the results chain for the government's program should be selected as DLIs, though monitoring the full results chain is important. The absolute number of DLIs for a P4R operation, and the selection of actions, outputs, and intermediate outcomes, should aim to balance the number of key milestones that are considered critical to keep the government's program on track in its results chain with maintaining a streamlined design for the operation (practicality and manageability).
- ***Can we measure the DLIs?*** The selection of the DLI should also take into consideration the practical aspects of measuring, monitoring, and verifying achievement of the result. DLIs should be clearly defined and measurable, with clear protocols for monitoring (as discussed below).

(c) Linkage with Disbursement

16. Disbursements would be made, at the request of the government, when the DLIs have been achieved and verified. It is anticipated that most P4R operations would support ongoing

government programs that are funded in the government's current budgetary process. Normally when the DLI is achieved and verified, the Bank would disburse the specified amount.

17. A key aspect of designing P4R operations would be the time calibration for expected achievement of results. This would depend on the expected timetable for progress in the specific result and the timing of data collection needed to verify achievement of results. Also, in some cases certain results may need to be achieved before the financing agreement is signed to permit implementation of the desired subsequent program results—for example, establishing credible baseline data or setting up the monitoring arrangements for the main program. In such cases, the Bank could agree to a set of DLI results to be achieved after the approval of the Project Concept Note as long as the aggregate amount assigned to DLIs achieved before the signing of the financing agreement does not exceed 20 percent of the amount of the financing, similar to what is in place for other lending instruments.

18. Another aspect is scalability of the DLIs. Depending on the program and type of indicator, DLIs could be designed to be scalable, with Bank disbursements proportionate to the progress achieved toward the associated program milestone. The decision of whether to design scalable DLIs needs to consider carefully the effect of a partial achievement of the program milestone on continued progress in the program's results chain, and the eventual achievement of the program's PDOs. Alternatively, the results chain could specify a series of "stepwise" DLIs to measure incremental progress toward achieving the results.

19. The amount allocated to the achievement of each DLI would support a defined program of overall government expenditures and would not be attributed to specific expenditures. In some cases, a government may need advance funds to achieve the initial DLIs. Provisions would be made for advances up to a specified amount of the total financing to be disbursed prior to the achievement of DLIs. Disbursements under subsequently achieved DLIs would be reduced by 15 percent of the amount due to be disbursed under those DLIs to recover part of the advance. The borrower would be required to refund to the Bank any advances not recovered from achieved DLIs by the closing date of the financing.

20. During the preparation of a P4R operation, the Bank would work with the government to develop and agree upon "protocols" for verifying the achievement of program milestones selected as the operation's DLIs. Each DLI should have a monitoring protocol that clearly sets forth the following:

- The definition of the DLI and how it will be measured.
- An objective and detailed definition of the elements needed to consider the DLI achieved, including a clear timetable for DLI achievement (with reasonable reference to the timing and frequency of measurement and data availability), and identification of the sources of data to be used in measuring the achievement of the DLI.
- Identification of the entity responsible for verifying achievement of the DLI. This entity may be an agency of the government (such as a line ministry providing verifiable administrative data, a national statistics office providing independent data that measures outcomes, an oversight agency, etc.). In some cases, verification may

depend on a credible external or third-party entity (e.g., an independent entity, autonomous or semiautonomous institutions, centers of excellence, NGOs, private sector).

21. For results achieved prior to the closing dates of the financing agreements, a period of 4 months after the closing date would be allowed for the verification protocols to be completed and for the government to request the related disbursement.

C. Systems Assessments

22. To make sure that funds are used appropriately under an expenditure program to be supported by a P4R operation and that the environment and affected people are protected, the Bank would assess the procurement, financial management, and other fiduciary aspects of the program, as well as the management of environmental and social impacts, using the key principles that underlie the Bank's assessment of all the operations it supports. Many of the assessment methodologies would build on and benefit from tools that have been developed for IL and on analytic work, and would take relevant international practice into account. The assessments would include (a) a qualitative review of the existing arrangements under the program; (b) a performance assessment of such arrangements, (c) identification of areas in which the implementing entities could improve procedures and performance, including a proposed action plan, as necessary; and (d) inputs to the risk assessment of the operation. These assessments would be integrated where possible, since they would all be examining how the program and its systems perform. Integrating the assessments would assist in identifying risks related to cross-cutting issues like governance, as well as needed actions/mitigation measures.

23. If the assessments conclude that the program processes are adequate and that the implementing institution(s) has(have) the capacity to implement the program, project preparation would proceed to approval, and the focus of the Bank's work would gradually move toward project implementation. If the assessments reveal material weaknesses, the Bank and the borrower would agree on measures to address them—for example, through the following options:

- Where the weaknesses are so severe that credible remedial measures at the program level are judged unlikely to work, the Bank may decide not to finance the operation or, if the risks can be better mitigated by another lending instrument, to use that instrument.
- Measures could be identified to improve capacity, systems, and procedures, and could be supported by the Bank loan, trust funds, or another donor, or from the client's own resources. Progress in implementing these measures would be monitored during implementation. Some would be in the form of legal covenants.
- In certain cases, the DLIs may include specific actions, including fiduciary and environmental and social matters, as results that would be monitored during implementation.
- Specific actions could be agreed for inclusion in an operations manual for the program or in the internal regulations of the client, all of which would be monitored during implementation.

Adjustments could be made to the terms of reference of the integrated audits and/or Bank monitoring during implementation to focus on the areas of weakness or riskiness.

24. During project implementation, Bank staff would monitor whether the arrangements used adhere to the agreements reached during project preparation. If a Bank team concludes that specific arrangements do not adhere to those agreements or that performance is lagging, it would notify Bank Management and the client, and ask that the client take timely and appropriate action. If program performance continues to lag over a long period of time for reasons within the control of the client,[3] the Bank would have the right to apply the relevant remedies, defined in the legal agreements.

1. Assessment of Fiduciary Systems

(a) Procurement

25. The **key principles** that underlie the procurement assessment are transparency, economy, efficiency, competition. These principles are traditionally associated with the concept of achieving value for money in public procurement.

- For example, *economy and efficiency* require (a) planning; (b) knowledge of relevant markets and prices; (c) aggregation of demand, as appropriate, to achieve the operational needs of the program; (d) coordination between commercial and technical aspects (specifications, design, cost estimates, spare parts, warranty, etc., as applicable); (e) competiveness (i.e., applying procedures that maximize participation and are compatible with technical requirements and market capacity); (f) efficient administrative procedures (i.e., without unnecessary delays or undue approvals); and (g) equitable and efficient contract administration (payment, resolution of claims and disputes, quality and cost control processes).
- *Transparency* would also help achieve value for money. It entails in particular: (a) clear rules, easily accessible and consistently applied; (b) wide advertisement of contract opportunities and awards; (c) decisions made only on the basis of rules previously disclosed for the specific procurement; (d) effective complaint resolution; and (e) reliable internal and external control processes. Open competition should be the preferred procurement method whenever it makes sense, with direct contracting used when clearly defined conditions for its use have been met.

26. ***Procurement Assessment Approach.*** A procurement capacity assessment would be carried out to determine whether the key principles (efficiency, economy, transparency, competition): (a) are facilitated by applicable rules and processes; (b) can be implemented with existing capacity and controls; and (c) are achieved in practice. The procurement assessment would not focus on "equivalency" with Bank rules and procedures. Rather, commonly accepted procurement attributes would be used to determine whether the procedures to be applied under the program are acceptable by reviewing how procurement is done and how it is controlled. Under the P4R, the assessment would be threefold:

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[3] To be determined on a case-by-case basis, but expected to be usually between 6 and 12 months.

- A qualitative review of the *procurement arrangements* for the program (i.e. applicable rules and procedures and capacity of the program's implementing agencies) to ensure their substantial consistency with the principles embedded in the Bank's Articles of Agreements. This review would build on the vast experience in undertaking procurement assessments in projects.
- A *performance assessment* focusing on how past procurement practices have contributed to achieving the procurement principles and how they would support the program's development objectives and outputs. Performance assessments would build on past experience in operations financed by the Bank and other development partners, as well as international best practice.
- A *risk assessment* to ensure that implementation arrangements are acceptable and risk is reasonably mitigated by the existing framework. The procurement capacity assessment would be a key input to the management decision on whether the program is appropriate for P4R and may include an action plan for helping counterparts to further enhance value for money within the overall program, as an additional development objective of the specific P4R operation. The risk assessment would feed into the overall risk assessment framework for the P4R operation. In recent years, the Bank has invested in specific risk assessment methodologies for IL and for procurement that will adapted for use at a program level.

27. The assessment would evaluate, among other things, the capacity of the implementing entity to administer procurement processes and contracts and to exercise relevant internal and external controls. It would also ensure the existence of a complaint review mechanism (key to bidders' participation and external accountability) and evaluate the integrity of the procurement processes. As much as possible, the procurement assessment would be integrated with the FM and technical assessments, in line with good practice for dealing with governance issues in Bank investment lending. Finally, the assessment would review whether the program is expected to finance some high-value and/or contracts over the P4R operation's implementation period.

28. ***Assessment of existing Procurement Arrangements.*** The assessment of procurement arrangements under the program would focus on the following key attributes:

(a) Procurement procedures are based on clear and enforceable rules—for example:

- Rules are easily identifiable and freely accessible to the public;
- Bidding opportunities are advertised widely;
- Open competition is the default approach, and conditions for all other methods are clearly described;
- Qualification, evaluation, and award criteria are clearly defined in bidding documents, which are relevant and nondiscriminatory;
- Contract conditions are equitable;
- Bidders have access to a complaints review mechanism; and

- The results of the procurement process are disclosed.

(b) Efficient planning processes exist—for example:

- Procurement planning is clearly linked to available budget and objective end-users needs;
- Planning is realistic and complies with applicable rules (e.g., procurement methods); and
- Procurement of goods and services is consolidated, as appropriate, for economy of scale.

(c) Effective external control, as assessed by the Bank team's FM specialist.

(d) Effective internal controls, including internal audit, clear definition and segregation of functions relevant to procurement, clearly defined accountability, quality control processes, and complete records of procurement processes.

(e) Adequate staffing in terms of numbers and experience to implement the program.

(f) Integrity of the procurement process:

- Rules setting clear ethics standards exist;
- Procurement decisions are made on the basis of established processes by competent authorities, and are generally not overruled;
- Bidding procedures adequately preserve the integrity of the process (e.g., there is a chain of custody of the bids, and evaluations are confidential); and
- There is a functioning complaints mechanism.

(g) Adequate processes and capacity for contract administration; the assessment would consider the following:

- Cost and time overruns;
- Quality control of goods, works, or services delivered;
- Timeliness of payment;
- Contractual dispute resolution; and
- Application of contractual remedies.

29. For programs involving several implementing agencies, the Bank team would assess the capacity of the agency nominated as the lead or coordinator for the program, and all those having a major role in procurement administration, or a representative sample of agencies if all play a similar role.

30. ***Procurement Performance Assessment.*** Assessment of the program's procurement performance would focus on past performance in implementing the program or similar programs, and would include a review of recent audits and of selected processes, and would draw from data generated by a management information system, if available, and/or performance audits carried out

during preparation. These reports would provide information on key performance indicators for each of the areas outlined above and would be used to guide the evaluation of implementation.

31. Measurable indicators would be used to assess and monitor procurement performance, including (a) the efficiency of the procurement process cycle, in terms of timeliness, openness, cost-effectiveness, and compliance with applicable rules; (b) the competitiveness, transparency, and efficiency of procurement planning; and (c) the level of competition and prices, combining cost information with proxies expected to affect prices. A baseline for each of these indicators would be developed to help monitor procurement performance during implementation.

32. Measurable procurement outcomes are context-specific because they are affected by multiple variables (market, capacity, location, risk, and political economy). Consequently, outcomes for a program would need to be assessed in the context of the country and, as appropriate, the sector. For example, prices paid for goods, non-consulting services, and works under the program would be compared with prices paid for the same or similar items by other government agencies in the country. A similar approach would be followed for the other two performance dimensions. Reasonable market prices would be calculated, taking into account simple variables such quantities procured, inflation, and delivery locations and conditions.

33. ***Monitoring of Procurement Arrangements.*** During project implementation, Bank teams would monitor whether the procurement arrangements used adhere to agreements reached during project preparation. If Bank teams determine that specific arrangements do not follow agreements reached during project preparation or that performance is lagging, they would notify Bank Management and the client, and ask that the client takes timely and appropriate action. If, as evaluated by Bank teams, and confirmed by Bank Management, the performance continues lagging over a long period of time for reasons within the control of the client,[4] the Bank would have the right to apply the relevant remedies, defined in legal agreements

(b) Financial Management

34. The **key principles** guiding the assessment of financial management (FM) arrangements are as follows:

- ***Support the program in improving its FM performance.*** The program FM arrangements would be designed to facilitate and promote sustainable development of the capacity of the implementing entities, promote efficiency and effectiveness, and help achieve the PDOs.
- ***Contribute to providing reasonable assurance on the use of all the program funds.*** FM staff would design and later supervise borrower implementation of Bank-financed operations to assess the adequacy of the implementing agency's FM arrangements, including budgeting, accounting, internal controls, fund flow, financial reporting, and auditing arrangements. If needed, appropriate mitigation measures, including institutional capacity strengthening, would be developed to address risks posed by weaknesses identified.

[4] To be determined on a case-by-case basis, but expected to be usually between 6 and 12 months.

35. ***Financial Management Assessment Approach.*** The objective of the FM assessment would be to determine whether the entities (or entities) that would execute all the program expenditures have acceptable FM arrangements.[5] FM focuses on all program funds, regardless of their source or managing institution. FM would also assess whether the program has an appropriate level of fiduciary controls. To enhance ownership, harmonization, and development results, the implementing entity's FM system would be used for the P4R operation. Therefore, the FM assessment would be carried out at the program level using information available from diagnostics conducted by the Bank or other donors. The focus would be on enhancements or additional controls needed to ensure that the FM systems are able to adequately support any specific accounting, reporting, auditing, and funds flow arrangements required for the operation. Approaches to strengthening the FM systems and addressing weaknesses may include support by ongoing public financial management reform initiatives; piloting the use of FM systems or strengthening measures at the sector level under the public financial management reform initiative; and financing and technical support.

36. The FM arrangements include the entity's system of accounting, reporting, auditing, and internal controls. The entity's arrangements are acceptable if they are considered (a) capable of recording correctly all transactions and balances, (b) supporting the preparation of regular and reliable financial statements, and (c) safeguarding the entity's assets, and if they are subject to acceptable auditing arrangements. The assessment would include establishment of an initial baseline that would be monitored throughout project implementation. The FM assessment would focus on the following key attributes of the program's FM arrangements:

(a) Budget:

- Arrangements for periodic budgets are consistent with the program strategy;
- Program plans and budgets are realistic, based on valid assumptions, and developed by knowledgeable individuals;
- Procedures are in place to plan program activities and prepare related budgets, and to collect information from the units in charge of the different components;
- Budgets are prepared for all significant activities in sufficient detail to provide a meaningful tool with which to monitor subsequent performance;
- Periodic budgets and cash flow projections are supported by approved procurement plans; and
- Cash flow projections are consistent with agreements reached with the Bank regarding the timing and frequency of program disbursements.

(b) Accounting:

- An integrated financial reporting system is being implemented;

[5] The assessment would build on the extensive experience acquired in carrying out assessments of FM arrangements for all IL projects, in conducting Country Financial Accountability Assessments, and in using tools developed with partners, such as the Public Expenditure and Financial Accountability reviews. It would also build on the experience obtained with already-approved loans that have a strong programmatic and results focus.

- The program's chart of accounts facilitates periodic and annual reporting of information relating to program activities; and
- Satisfactory periodic reports are prepared for purposes of accountability and reporting on program implementation progress.

(c) Financial reporting:

- The program has established and documented financial reporting responsibilities that specify what reports are to be prepared, when they are to be prepared, and what their content and periodicity should be; and
- The financial reports compare actual expenditures with budgeted and programmed allocations.

(d) Internal controls:

- The program has an institutional risk management policy framework that sufficiently takes account of fiduciary risks at various levels;
- The implementing agency has an independent oversight team with clear responsibility for risk management activities, including (a) the proper use of program resources, (b) timely accountability and reporting by management, and (c) timely implementation of internal control strengthening recommendations; and
- The program has an internal audit unit that is sufficiently independent and resourced to cover all program activities, or there are satisfactory arrangements for periodic independent review and verification of program activities.

(e) External audit:

- A competent and independent supreme audit institution audits the activities of the program;
- The program's financial statements are audited regularly by an independent auditor; and
- The audit of the implementing entity is conducted in accordance with acceptable standards.

37. The FM assessment would also cover governance-related issues by, for instance, identifying gaps or weaknesses in internal controls that create opportunities for corruption. The focus would be on not only the design of internal controls but also how they operate in practice. The FM assessment of risks should factor in such governance risks as (a) the risk environment at the country, sector, and program level; and (b) risk factors that are specific to the program concept, for example, implementation through decentralized local bodies or NGOs that have weak capacity or lack of accountability. Tasks identified at the country and sector level will often play out differently at the program level; therefore, the assessment would need to include program-specific information about the risks, including (a) implementing entity audit reports and management letters, (b) previous FM assessments of the implementing agencies, and (c) information from project supervision and any reports available from INT.

38. ***Monitoring of FM Arrangements.*** As part of implementation support, FM staff would monitor the system assessed to determine any material change in its performance. They would also monitor progress on implementing any agreed risk mitigation measures, and review financial reports (and audits of them) that confirm whether agreed expenditures, at the appropriate level of aggregation, had been financed by the loan proceeds. FM staff would:

- Provide technical support and monitor the continuing adequacy of the FM arrangements;
- Follow up on action plans and the FM-related indicators agreed during project appraisal/negotiations, as well as on observations derived from reviews of audit reports, management letters, and program progress reports;
- Work with the borrower to identify and resolve FM implementation issues, providing advice and technical support, including capacity building, to ensure smooth implementation of the program and good performance of the program FM arrangements; and
- Help the client implement FM related governance strengthening and risk mitigation measures that are part of the program design—including, as necessary, strengthening the client's internal control systems, enhancing transparency and disclosure of financial information, supporting accountability and oversight mechanisms, and building client capacity in these areas.

2. System to Manage Environmental and Social Impacts

39. The assessment of the program's system for managing environmental and social impacts would be based on the following **key principles**:

- Avoiding or minimizing potential impacts and risks of program activities for the socioeconomic, physical, and biological environment,[6] with due consideration to vulnerable groups including, but not necessarily limited to, indigenous peoples.
- Avoiding or minimizing involuntary resettlement and assisting displaced people in improving or restoring their livelihoods to pre-displacement levels.
- Conserving, maintaining, and rehabilitating natural habitats and their functions, or supporting efforts to realize the potential of forests to reduce poverty in a sustainable manner by integrating forests into sustainable economic development.
- Protecting physical cultural resources of archaeological, paleontological, religious, aesthetic, or historic value.

These environmental and social principles would be used not as benchmarks for prescribing remedies but rather as a means to evaluate how the government program is designed to identify, avoid, minimize, mitigate, or compensate for such risks and impacts.

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[6] These considerations include adequate treatment of safety of dams, pest management, international waterways, and projects in disputed areas.

40. ***Environmental and Social Impact and Risk Management Assessment Approach.*** The assessment of the system to manage environmental and social impacts would include (a) a review of existing arrangements or current practices under the program to manage environmental and social impacts; (b) an assessment of capacity to implement the system; and (c) a risk assessment, including a risk mitigation plan, that would feed into the overall risk assessment framework of the P4R operation. More specifically, the Bank would:

(a) ***Review existing legal and regulatory requirements*** that apply to the program to determine whether they are sufficient to meet the principles outlined above.

(b) ***Assess the capacity to plan and implement*** the applicable environmental or social mitigation measures and to monitor and report on the effectiveness of mitigation measures that may have already been undertaken. As part of the capacity assessment, staff would obtain independent information through discussions with civil society organizations, other program supporters, or others who have had relevant experience in engaging with agencies involved. Major points of focus would include the following (more guidance will be provided on the methodology for carrying out a capacity assessment through staff Guidance Notes):

- *Technical:* for example, availability of qualified and experienced personnel who are able to perform technical planning and mitigation tasks.
- *Procedural**:*** for example, whether program processes are transparent, responsive and accountable. Consultation arrangements should allow for plans and service standards to be influenced by the affected public; disclosure arrangements should provide adequate and timely information to the interested public; and grievance redress mechanisms should provide an effective and efficient first-recourse means to identify and address grievances within the program.
- *Organizational**:*** for example, whether program agencies have the authority and budget to act effectively, and whether adequate coordination arrangements are in place if multiple agencies are involved in planning or mitigation.

If significant capacity gaps are identified, capacity building activities would be identified and included in the risk mitigation plan (see below).

(c) ***Assess the risks to implementation,*** taking into consideration the principles outlined above, the capacity assessment, the likelihood that potential adverse social or environmental impacts will occur, and the applicability of the following environmental or social risk flags:

- Environmental impact risk flags:
  - Physical investments generating immediate or cumulative environmental impacts that are multidimensional, unprecedented, or irreversible, or for which effective mitigation measures are not known, or that cannot be limited to the immediate investment area.
  - Carbon-intensive activities, or those increasing air or water pollution, or requiring management of large-scale or sensitive waste materials.

  - Changes in land use that would involve conversion or degradation of natural habitats, biodiversity loss, loss of natural forests, or impact on physical and cultural properties.
  - Manufacture, use, storage, transport, or disposal of pesticides, toxins, or other hazardous materials.
- Social impact risk flags (potentially severe or complex social impacts are necessarily more contextual, requiring greater application of judgment in determining how, or if, the P4R instrument can be applied appropriately in a given program context):
  - Identifiable risks to human health or safety potentially affecting communities, workers, or other large groups.
  - Identifiable potential for generating social conflict, especially in fragile states, post-conflict areas, or areas subject to territorial disputes.
  - Activities affecting indigenous peoples communities, especially for activities imposing changes in rights or access to natural resources, commercial development or exploitation, or physical relocation.
  - Acquisition of production land that would cause economic dislocation (e.g., people would need to relocate to resume production or, alternatively, would need to undertake different activities to improve, or at least restore, livelihoods).

41. As part of the assessment, a risk mitigation plan would be developed that would identify the range and complexity of potential environmental and social impacts that may be involved in the program, the measures to be used to mitigate them, and the specific outcomes to be obtained. The client and the Bank would agree on specific environmental or social mitigation results to be achieved, on objective indicators, and on any institutional arrangements deemed necessary for effective impact mitigation. These arrangements would be incorporated, as relevant, into the operational manual or other program guidance and, within the Bank, would be reflected in the Project Appraisal Document (PAD) and legal documentation. The risk mitigation plan would also specify agreed steps to enhance the program's environmental and social performance of the program and hence its sustainability, and to strengthen the technical, procedural, or organizational capacity to implement the plan, if warranted. If any of the environmental or social risk flags are deemed relevant to the proposed program, the Bank would ensure that the program includes specific and objectively monitorable mitigation measures among program results.

42. ***Specified mitigation results would be commensurate with the potential severity of risk***. When client programs have the potential to generate social risk, it is expected that a robust, well-documented grievance mechanism would be an integral part of the client's risk management program. Also, more significant risks would require greater Bank attention.

43. ***Consultation and Disclosure.*** The assessment process itself would include a stakeholder consultation with the objective of testing the findings of the draft assessment against the knowledge and perceptions of stakeholders who are involved in the government program. Relevant information regarding environmental and social issues would be disclosed via an enhanced Project Information Document (PID), replacing the Integrated Safeguards Data Sheet

that was designed specifically for IL operations. The PAD would describe the potential environmental and social impacts, program capacity to mitigate impacts, and capacity-strengthening or other specific measures deemed necessary to ensure effective performance. The PID would summarize potential impacts and mitigation arrangements described in greater detail in the PAD. Both PID and PAD would be disclosed in accordance with the Bank's Access to Information Policy.

44. ***Monitoring of Social and Environment Management Arrangements.*** Consistent with the increased emphasis on actual program results, the Bank would actively support client implementation and verify program performance. Measures to assist client implementation may include provision of technical assistance, support for supplemental training, identification of qualified and experienced consultants, and participation in monitoring or evaluation processes as requested.

45. During implementation, the client would monitor and report on the environmental and social aspects of program performance through its regular monitoring, the grievance mechanisms, and an annual audit in keeping with parameters established in the risk mitigation plan. The Bank team would discuss the findings of the audit and, as appropriate, undertake random or occasional field performance reviews, including consultation with directly affected people. The Bank team would also routinely review the effectiveness of grievance monitoring and redress processes: the institutional functionality of the system, its responsiveness to grievances that may arise, and information feedback from recurring grievances into system management.

46. In complex programs, complaints regarding relatively minor system malfunctions or unanticipated circumstances are very likely to occur. When the Bank observes relatively isolated implementation problems, it would bring them to the attention of the program implementing agency. If patterns of failure are observed, or if previously identified problems are not addressed in due course by the government, the Bank would view such circumstances as indicating some degree of program failure requiring more systematic attention. Some cases, however, may reflect localized or systemic failures of commitment, which may require application of stronger remedies. The Bank's recourse scheme would be as follows:

- ***Marginally substandard performance:*** Remedial actions, proportionate to inherent environmental or social risks, would be agreed and specified in the Implementation Status and Results report. Remedial actions would include measures to rectify environmental or social harm that may have occurred, as well as steps to reduce the likelihood of recurrence.
- ***Continuing substandard performance:*** If progress in remedying shortcomings is lacking or insufficient, a timetable for remedial actions would be established and linked to specific sanctions.
- Limited or localized program compliance failure resulting in significant harm or threat of significant harm: The Bank would apply a targeted, localized sanction linked to disbursement or program eligibility.
- ***Systemic failure resulting in significant harm or threat of significant harm:*** The Bank would apply a program sanction in the form of halted disbursement or, in the case of prolonged noncompliance, recourse to legal remedies.

3. Integrated Audits Arrangements

47. The scope of Bank monitoring under P4R operations is expected to be broad, both in terms of the large number of activities likely to be under way at any time under the government programs, and in terms of the number of areas (e.g., procurement, FM, governance, and environment and social) where monitoring will be required. Since the assessments in these areas are closely related, integrated audits would be used to assist clients and task teams to monitor performance and implementation of the measures agreed during preparation, and to assist in verification of some DLIs for which verification is best done through an audit.

48. ***Scope of the Integrated Audits.*** Specific terms of reference for the audits, developed jointly by procurement, FM, environment and social staff, and the team leader, would be agreed with the client and would typically include the following:

- Overall compliance with applicable rules;
- Follow-up on agreed actions, including those in the risk mitigation plan to manage environment and social impacts and risks of the program;
- Assessment of overall value for money for procurement under the program, using proxy indicators;
- Overall efficiency of administrative activities and management policies;
- Overall efficiency of the use of human, financial, and other resources (e.g., information systems, monitoring arrangements, procedures followed by entities to remedy performance issues identified by audits);
- Physical inspections assessing quality of goods and works and the reliability of grievance mechanisms; and
- Verification of outputs linked to disbursement, as feasible (teams will indicate for each DLI the appropriate verification protocol).

Monitoring and verification of some results may be included in such audits, but as these are usually handled by different institutions, the design would be flexible and the key would be to ensure the reliability of the information needed for various aspects of the program while maximizing the integration of the audits.

49. ***Who Conducts Program Audits?*** Auditors should act with integrity, impartiality, objectivity, competence, and professionalism. The Bank would assess the capacity of the country's supreme audit institution (SAI) and the program's internal audit functions to ensure high quality of work, relevance, and independence.

- ***SAI:*** In most of the Bank's member countries, constitutional or legal arrangements provide for an SAI to report on the management of public funds by the executive branch and to support the legislature in holding the executive accountable for this management. If the SAI has sufficient capacity and independence in its funding, in setting audit programs, in carrying out its work, and in making its findings public, the Bank should consider it in deciding on the audit arrangements for the program.

- ***Internal audit:*** Internal audit is an independent, objective assurance and consulting activity designed to add value to and improve an organization's operations. It helps evaluate and improve the effectiveness of risk management, control, and governance processes. Independence is established by the organizational and reporting structure, and objectivity is achieved by an appropriate mind-set. The internal audit activity evaluates risk exposures relating to the organization's governance, operations, and information systems, in relation to (a) the effectiveness and efficiency of operations, (b) the reliability and integrity of financial and operational information, (c) safeguarding of assets, and (d) compliance with laws, regulations, and contracts.
- ***Independent verification agents:*** This category may include consulting firms with appropriate experience and capacity.

If the assessment of the SAI or the internal audit concludes that they have adequate capacity and independence, the Bank would place reliance on their work and agree with them on detailed terms of reference for the assignment. If the assessment reveals material weaknesses, the Bank would agree with the borrower on alternative measures to address the audit aspects—for example, to develop an action plan to enhance the audit capacity, or to rely on independent verification agents.

D. Risk Assessment Framework

50. At different points in the P4R operation's cycle, the Bank, with government inputs, would undertake a risk assessment to identify the major risks to the program's achieving its stated results, determine appropriate mitigation measures, and monitor the evolution of risks, the implementation of mitigation measures, and their impact.

51. The risk assessment framework would be similar to the Operational Risk Assessment Framework used in IL operations and would help the government and the Bank make a systematic, holistic, and integrated evaluation of the risks that the program may not achieve the expected results over the implementation period of the P4R operation. The framework would be used from preparation through implementation. During preparation, the framework would be used to (a) identify the most important risks and design mitigation measures that would be applied during preparation or implementation; (b) follow the progress in implementing those measures; and (c) work with the government to adjust them as necessary. During implementation, the framework would be used to regularly scan the spectrum of possible risks to help the government move quickly to identify and address emerging issues, including unanticipated risks. The framework would include the following major risk categories, at the program level:

- ***Program-related risks:*** technical soundness, financial and economic risks; fiduciary, environmental, and social risks; and performance risks.
- ***Institutional risks:*** institutional arrangements, capacity and governance risks.

- ***Country-level risks:*** the country's politics and governance, societal, and security issues, economic management issues that may affect the program's ability to achieve the expected results.
- ***Stakeholder risks:*** the direct and indirect stakeholders who might affect the program's ability to achieve results.

52. The Bank, in consultation with the government, would rate each risk category, taking into account two dimensions: likelihood and impact. On the basis of these ratings, the Bank would derive an overall program risk rating. The government and the Bank would then agree on key mitigation measures to be carried out during preparation and/or implementation of the P4R operation; those that take place during preparation may change the overall program risk assessment during implementation. To be effective, mitigation measures should be few, specific, and time-bound, and their implementation should be monitored continuously by the government and the Bank. If a mitigation measure cannot be implemented or is found not to have the intended impact, the government and the Bank may agree on an alternative measure.

53. The initial risk assessment, the associated risk mitigation measures, and the overall program risk rating would be used at the P4R operation's Concept Review to help determine the level of Management scrutiny, including whether a corporate-level review is required. The risk framework would be updated during the preparation phase based on the above-mentioned technical and systems assessments and growing knowledge, and during the implementation phase to reflect task teams' findings.

54. The Concept Review would determine the level of corporate review and decision making during the preparation phase. If Management deems the overall program risk to be too high relative to the results expected under the program, Management may decide not to move ahead with preparation of the operation, to prepare an IL or DPL operation instead, to provide support through provision of technical advice, or not to provide any support at that time. If the P4R operation is to proceed, then the overall risk assessment, with the proposed mitigation measures, would be an input to Management's decision on the level of corporate oversight and Bank resources to be allocated through the project cycle, including for implementation support. The risk assessment would be updated regularly, and the mitigation measures would be one focus of implementation support.

ANNEX C: DRAFT CONSULTATION PLAN

1. The World Bank is developing a new approach to results-based lending—the Program-for-Results (P4R) lending instrument—that it expects to roll out in 2011. To inform the development of the P4R, the Bank will seek the views and input of a wide array of stakeholders. A global consultation process will begin around March 2011, after the Bank's Executive Directors discuss the P4R concept note. This note sets out a draft plan for the consultations.

I. CONTEXT

2. The World Bank's business model and products continue to evolve. Clients are seeking—and Bank staff are developing—new and innovative lending approaches that are more flexible and provide quicker and more customized solutions. Today the Bank provides financing to its clients through two lending instruments: investment lending (IL) which supports specific projects and disburses against specific transactions, and development policy lending (DPL) which supports institutional and policy reforms.[1] The proposal to introduce a new program lending instrument emerged from the Bank's IL reform process. As part of the March 2010 IL reform update, Management indicated its intention to propose such an instrument, which would focus on a "program orientation" approach as a complement to the "transaction-based" approach of traditional IL. The Bank is now working to design the P4R—a results-based lending instrument that would support a government's program in particular sectors or subsectors with a clearly defined results framework. The P4R will be based on results, not inputs, and will focus on strengthening institutions and capacity, while ensuring that Bank financing is used appropriately and the possible social and environmental impacts and risks of the program are adequately addressed.

II. CONSULTATION OBJECTIVES

3. The purpose of consultations is to elicit input and feedback from a wide range of stakeholders, in as broad and inclusive a manner as possible, to help the Bank formulate the new lending instrument.

4. ***Shareholder and Stakeholders.*** The consultations will include representatives of governments, international organizations, multilateral development organizations and banks, United Nations agencies, parliamentarians, the private sector, civil society, foundations, academia, think tanks, and practitioners.

5. ***Objectives***. By engaging a wide range of stakeholders, the consultation process will aim to:

- Raise awareness about the rationale for the P4R and inform the stakeholders about the concept.
- Provide information and guidance on the potential benefits this new instrument will bring to clients, borrowers, and the Bank's key stakeholders.

[1] In addition, the Bank also offers guarantees in the context of mobilizing private sector finance.

- Create a space where stakeholders can provide input and feedback on how to move this instrument forward.
- Elicit feedback: listen to stakeholders' views and concerns regarding the P4R.
- Establish a dialogue and relationship between the World Bank and key stakeholders so that implementation of the instrument can continue to benefit from diverse perspectives.

III. Consultation Process

6. The consultation process on the P4R Concept Note—which forms the basis for the new program-based instrument—is expected to begin in March 2011, and the inputs received from stakeholders will inform the design of the P4R instrument. During the pre-consultation period, we will make available a wide range of materials to support the consultations.

A. Pre-consultation

7. Before the start of consultations, we will update, translate, and post documents, communicate with key stakeholders, and make key information easily available and accessible. This will provide interested stakeholders sufficient time to formulate their thoughts and opinions on the proposed instrument so that they will be ready to provide substantive feedback in face-to-face and web-based consultations on the P4R Concept Note. A calendar of events highlighting outreach opportunities will capture the range of the consultations.

8. ***Website.*** We will launch a dedicated website (www.worldbank.org/P4R), providing information on the consultation process and key materials that stakeholders can consult and download:

- The P4R Concept Note (in Arabic, Chinese, English, French, Russian, and Spanish).
- Links to additional background information on IL reform, its pillars, and its milestones.
- An outline of the overall consultation process:
  - The Consultation Plan, with countries identified as they are selected.
  - Consultation calendar/schedule, updated constantly to show the city/country where a meeting will be held, date, type of consultation (open, restricted), and possibility for stakeholders to sign up to attend open consultations.
  - Discussion questions that will be used to frame the consultations

We will also use the website to notify stakeholders about the consultations one month before they begin. Visitors to the site will be able to sign up to be notified when significant updates are posted on the site. In addition, interested stakeholders will be able to use the webpage to contact the IL consultation team with any questions on the process or the available information.

B. Consultations

9. Through the consultations we will seek input and feedback on the P4R Concept Note. External consultations will involve a combination of web-based (through a global web platform) and face-to-face consultations: videoconferences, global meetings, and targeted face-to-face meetings in various countries. Internal consultations will be held during the same period.

1. Web-Based Consultation

10. From March 2011 onwards, individuals and organizations will be able to provide inputs and comments on the P4R Concept Note through a web-based platform that will include a web form and a designated e-mail address for those who wish to send comments via e-mail. All comments received electronically will be posted on the consultation web page.

2. Face-to-Face Consultations

11. Global consultations are planned in Washington, DC, Europe, and one Region. In addition, face-to-face meetings will be held in each Region, in a total of about 30 countries and at the regional level. For each consultation, we will strive to invite a balanced range and representation of stakeholders to participate, and we will provide proper notice of the meeting. These meetings will be led by Bank country directors.

12. Videoconferences will also be held with stakeholder groups in each Region to extend the reach of the consultations and ensure a more extensive geographic representation of stakeholders. In addition, country offices will arrange meetings with selected groups in partnership with local authorities and civil society organizations, universities, research institutions, and other local organizations with contacts throughout the country. Separate consultative meetings with governments/ministries will be arranged.

13. After each consultative meeting, the Bank will post on the website a summary of the comments. Visitors to the website will also be able to sign up to be notified when significant updates are posted on the site.

C. Incorporating Feedback

14. After the consultations end, the Bank will use the information and input gathered during the consultation process to inform the design of the new instrument. A document outlining how the issues raised during the consultations were addressed in the drafting of the proposed new instrument will also be posted on the site.

15. ***Feedback to Stakeholders.*** We will create, and post on the website, an overall feedback matrix summarizing all the feedback received. We will also post a summary of the key issues raised during this phase, along with Management's response and the next steps in the process (i.e., Board discussion or approval).

D. Final Steps

16. Once the Board approves the new instrument, we will share the final document widely and with all participants in the consultation process through e-mail and the webpage.