Overview:

LICUS

• Countries, Criteria
• Challenge
• Business models
• Core Principles
• LICUS Trust Fund
• Other funding support

• LICUS PFM challenge
  • Establishing Country PFM systems: Case study: Timor Leste
  • Improving Country PFM systems: Case study: Liberia

• The way forward
LICUS (Low Income Countries Under Stress):

<table>
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<tr>
<th>Severe (CPIA &lt; 2.5)</th>
<th>Core (CPIA 2.6-3.0)</th>
<th>Marginal (CPIA 3.1)</th>
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<td>Guinea-Bissau</td>
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•Criteria:
  
  - **Income**: FY05 list created using FY04 threshold of <$865 GNI.
  
  - **CPIA score** (Country Policy and Institutional Assessment): Score of <3.0 on both the overall and governance CPIA averages.
  
  - Plus low income countries without CPIA data – Afghanistan, Liberia, Myanmar, Somalia, Timor-Leste and Kosovo.
LICUS Challenge:

- These are the countries that need the most support:
  - Child mortality double other low income countries (LIC)
  - Malaria death rate three times other LIC’s
  - Three quarters are conflict affected
  - Aid twice as volatile as other LIC’s.
  - Aid programs have performed poorly
  - LICUS may cause adverse global spillovers
  - High fiduciary concerns
  - Poor outlook: The probability of a sustained turnaround in any year is 1.79%.
Fiduciary Challenge:

- LICUS countries have some of the most challenging fiduciary environments:
  - Incomplete legislative and regulatory frameworks
  - Weak institutions
  - Budget formulation inefficiencies
  - Budget mismanagement
  - Opaque internal controls
  - Widespread corruption in procurement
  - Delayed or incorrect monthly / annual reporting
  - Ineffective audit.

- Can LICUS country FM systems provide adequate assurance regarding use of Bank funds?
- What are the risk – return tradeoffs?
LICUS:

- LICUS Unit Background:
  - June 2002: Report presented to the Board. Task Force recommended that the Bank maintain a more consistent engagement with LICUS countries.
  - October 2002: LICUS Unit established in OPCS.

- LICUS Trust Fund:
  - Initial funding of $25 m. Term of three years for disbursement
  - Support for countries in non accrual status
  - Results indicators:
    (i) 50% of LICUS countries in non accrual show improved policies and institutions within 3 years (CPIA / PCIA),
    (ii) At least 25% of 2004 non-accrual engage with international donors through a structured arrears clearance process within 3 years,
    (iii) 75% of non-accrual countries have agreed multi donor approaches in place in 3 years,
    (iv) At least 1:1 ratio of co-financing or parallel financing of Bank assistance strategies from other donors.
LICUS - Core Principles:

• Within countries:
  – Stay engaged
  – Anchor strategies in stronger socio-political analysis
  – Promote domestic demand and capacity for positive change
  – Support workable and simple entry-level reforms
  – Explore innovative mechanisms for social service delivery
  – Focus on capacity building to support governance reform
  – Work closely with other donors

• Within the Bank:
  – Increase financing of AAA and capacity building work
  – Disconnect BB from lending volumes
  – Deploy experienced staff in LICUS
  – Review OP’s to assess applicability to LICUS environment
  – Provide support from OPCS to regional teams for strategy development and implementation
OECD DAC Fragile States Model:

- Strong or significant country leadership
  - Afghanistan
  - East Timor
  - Sudan
- Strong leadership from lead donor
  - Sierra Leone
  - Solomon Islands
  - Papua New Guinea
- Weak leadership / fragmented donors:
  - Nepal
  - Cambodia
  - Tajikistan
  - Central African Republic
  - Republic of Congo
- Most difficult contexts:
  - Myanmar
  - Burundi
  - North Korea
  - Angola
Bank LICUS Business Models:

- Prolonged political crisis (Somalia):
  - Disconnect between government and international community.
  - Bank’s focus is to rebuild rebuilding the stock of country knowledge; supporting national dialogue, capacity building, and where appropriate “ring-fenced” social service delivery.

- Fragile Transition (CAR, Liberia, Haiti, Sudan):
  - Peace process, reconciliation started, re-engagement with donors
  - Bank’s focus is to help create joint results framework and preparing for full IDA re-engagement through grant-based capacity-building, demonstration projects, and action on public finances.

- Slow progress (Cambodia, Tajikistan):
  - Weak governance without any immediate risk of instability
  - Bank’s focus is on implementing highly selective and harmonized strategies; identifying politically feasible reforms, and undertaking capacity building in high-impact areas.

- Deteriorating Governance (Eritrea, PNG):
  - Policies and indicators are deteriorating
  - Bank’s focus is on monitoring early warning indicators; faster CAS reorientation; more diagnostics.
Conflict Affected countries:

- Those which have recently experienced, are experiencing or are widely regarded at risk of experiencing violent conflict. Countries identified by regions. Coordination through Conflict Prevention Unit in ESSD
- Support from Post Conflict Fund (PCF). Established in 1997. Funding of $57.5 m from DGF and $5.8 m. from donors. Has approved 136 sub grants to 34 jurisdictions. Funding can be provided pre arrears clearance.
- Only 5 of 13 LICUS recipients are not PCF grant recipients

Post Conflict countries:

- Subset of conflict affected countries.
- Defined by FRM in terms of eligibility for exceptional IDA allocations as determined by Post Conflict Progress Indicators.
- For IDA 13 upto 40% of IDA allocations can be used as grants to establish main functions of governance and rebuild infrastructure, once arrears cleared. Exceptions established for prolonged arrears, state failure.
- FY05: Afghanistan, Angola, Burundi, DRC, ROC, Timor Leste.
Other LICUS support:

- **“Focus”** countries:
  - Bank classification based upon request for country departments for intensive Bank support.
  - FY03 focus countries: Angola, Central African Republic, Haiti, Papua New Guinea, Somalia, Sudan, and Tajikistan. FY04 these were Burundi, Comoros, Guinea Bissau, Liberia, Togo, and Zimbabwe and in FY05 these are Cambodia and Nigeria

- **JPCF countries**:
  - Japan Post Conflict Fund (JPCF) administered by PHRD and PCF Secretariat. PCF expected to provide smaller grants, while larger grants funded by JPCF.
  - Results have been mixed. Some support provided to Cambodia and East Timor.

- **MDTF countries**:
  - Bank administered multi donor trust funds channel resources to conflict affected countries - West Bank and Gaza, Bosnia, Kosovo, East Timor, Sierra Leone, Great Lakes region, Afghanistan, Iraq.
  - Countries financed under TF’s are also some of the largest recipients of post conflict funds.
**Case Study: East Timor**

- August 1999 independence referendum led to widespread violence.
- October 1999: UN Transition Administration for East Timor (UNTAET) took over responsibility for administering the territory during transition.
- October 1999: UN Joint Assessment Mission (JAM) undertook needs assessment and prepared results matrix. JAM covered eight sectors and identified priority areas for short term reconstruction and estimated external financing requirements.

**PFM arrangements:**

- PFM capacity building shared between different donors. Two principal funding mechanisms:
  - **Consolidated Fund for East Timor (CFET):** managed by UNTAET used to finance recurrent expenditures, civil service and capacity building. CFET resources formed part of the budget.
  - **Trust Fund for East Timor (TFET):** under trusteeship of World Bank, and used to fund economic and reconstruction activities. World Bank and Asian Development Bank were the two implementing agencies under TFET which operated outside the budget.
LICUS challenge: East Timor

PFM arrangements (contd.):
– Bilateral donors, UN Agencies, NGO’s provided assistance directly outside the framework of the Trust Funds.
– Capacity building the responsibility of operating staff

Achievements:
– World class PFM systems introduced and successfully implemented in East Timor.
– High level of fiduciary assurance.
– Effective commitment controls, cash management, internal and external controls for the government system.
– Clean audit opinion every year from leading global accounting firm.
– HIPC Assessment: In 2004 country met 14 out of 15 HIPC benchmarks. With PETS underway, in 2005 the country is likely to meet all 15 benchmarks.
Challenges:

- The development budget has remained outside the “government” system. Currently there are 7 large PIU’s, 8 small PIU’s and 58 other donor projects.
- Systems supplied by different donors operate in silos. The treasury system, procurement, asset management, inventory management, payroll, planning, customs, budget formulation or district management systems are not integrated.
- Over the last three years budget execution has reduced from 82% to 77% to 62% on a cash basis. The Ministry of Education had a budget execution rate of 25% in FY04, with 0% of the capital budget being spent. On a commitment basis, execution rates were over 90%.
- Effective payment system is not operational in the districts. Due to this, districts only hold petty cash.
- Even though 79% of the population is fluent in Tetun, 2% in Portuguese and the remaining in Indonesian, all PFM systems are in English.
- The PFM system is largely dependent upon expatriates. With UNTEAT phasing out in May 2005, sustainability is an issue.
- Capacity building efforts have had limited impact.
LICUS challenge: Liberia

Background:
- History of intensive donor support for PFM improvement
- Widespread mismanagement of public finances
- Under several recent regimes - very large revenue leakages (some booked as “pre paid receipts”)
- Expenditures incurred in non transparent manner (“Special commitment of the President”)
- Peace Agreement in October 2003. NTGL formed.
- UN JAM Mission in December 2003
- Successful Donor’s meeting March 2004

Achievements:
- Improvement in fiduciary environment from days of previous regime
- Halt to “Letter payments”.
- Payment system: MoF-UN-WB initiative to start payment of salaries in counties through UN in order to improve public service delivery.
- Payroll software: Effective local solution found.
- Good donor co-ordination: EU, IMF, World Bank, UST.
Challenges:
- Revenue leakages
- Excessive allocations
- Multiple expenditure controls: 33 stages
- Poor budget execution
- Large variations in monthly expenditure reports
- Lack of policy framework for Cash Management Committee (CMC)
- Institutional tensions
- Constrained Auditor General
Some progress:

- Bank proactively engaged in addressing LICUS Challenge
- Results focused
- Cross sectoral Bank teams working better for undertaking diagnostics and following through on implementation
- Building on past experiences:
  - MDTF structures improving – East Timor, Afghanistan
  - Advice re. institutional arrangements improving: West Bank, Afghanistan
- Bank surplus available for meeting short term needs esp. for countries in non accrual status
- Flexibility combined with fiduciary controls permitted DPL’s to Afghanistan, Haiti
- Policy framework being modernized: OP 8.50
How can we do better?

- Improve our understanding of country context and dynamics,
- Lower our expectations and be prepared for the long haul and the setbacks,
- Increase cross regional experience sharing
- Actively encourage increased use of country systems in LICUS countries
- Identify and invest in risky but sustainable local solutions
- Provide adequate funding and road map for capacity building upfront.
- Delink it from operational responsibility.
- Focus on harmonization in the field.
- Ensure that the limited country capacity is not diverted for harmonizing donors:

  “as Finance Minister I spent 60% of my time co-ordinating donors.”

  Ashraf Ghani, Former Finance Minister of Afghanistan, January 2005.