

**Assessment,
Afghanistan Reconstruction
Trust Fund (ARTF)**

Final Report

Oslo, March 2005



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Abbreviations

AACA	Afghanistan Assistance Coordination Authority (now abolished)
ADB	Asian Development Bank
AEP	Afghanistan Expatriate Project
AFA	Afghanistan Afghani (national currency)
AFMIS	Afghanistan Financial Management Information System
ARDS	Afghanistan Reconstruction Development Services
AREU	Afghanistan Research and Evaluation Unit
ARS	Administrative Reform Secretariat
ARTF	Afghanistan Reconstruction Trust Fund
CAO	Control and Audit Office
CD	Capacity Development
CDC	Community Development Committee
DAB	Da Afghanistan Bank (Central Bank)
DAD	Donor Assistance Database
DBU	Development Budget Unit (MOF)
DFID	Department for International Development
IARCSC	Independent Administrative Reform and Civil Service Commission
IDB	Islamic Development Bank
IDP	Internally Displaced Person
IMF	International Monetary Fund
LEP	Lateral Entry Program
LOTFA	Law and Order Trust Fund of Afghanistan
MAC	Ministerial Advisory Committee (for Administrative Reforms)
MC	Management Committee (ARTF)
MISFA	Microfinance Investment Support Facility for Afghanistan
MIWRE	Ministry of Irrigation, Water Resources and Environment
MoC	Ministry of Communications
MoE	Ministry of Education
MOF	Ministry of Finance
MOFA	Ministry of Foreign Affairs
MoH	Ministry of Health
MoWP	Ministry of Water and Power
MPW	Ministry of Public Works
MRRD	Ministry of Rural Rehabilitation and Development
MUDH	Ministry of Urban Development and Housing
NDF	National Development Framework
NEEP	National Emergency Employment Program
NGO	Non-Governmental Organization
NPP	National Priority Program
NSP	National Solidarity Program
O&M	Operations and Maintenance
PAREM	Public Administration Reform and Economic Management (program)

Scanteam:
Assessment, Afghanistan Reconstruction Trust Fund

PCN	Project Concept Note
PFM	Public Finance Management
PIP	Public Investment Program
PIU	Project Implementation Unit
PMU	Policy Management Unit (Office of the President)
PPU	Procurement Policy Unit
PRR	Priority Reform and Reconstruction (program/decreed)
PRS/P	Poverty Reduction Strategy (Paper)
SAF	"Securing Afghanistan's Future" (GOA strategy document, 2004)
SAI	Supreme Audit Institution
SY	Solar Year
UNAMA	United Nations Assistance Mission to Afghanistan
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
UNOPS	United Nations Office for Project Services
USD	United States Dollar
WB	World Bank

Note: After the elections of the fall of 2004 and with the creation of the new Cabinet as of early 2005, some ministries have been restructured and thus have been given new names. In order to maintain consistency, and because the period under review does not go beyond the 2004 elections, the former ministry structures and names are used throughout.

Exchange rate:

USD 1 = AFA 42.75 (approximate rate, January 2005)

Solar Year (SY):

Afghanistan's fiscal year, the Solar Year (SY), begins around March 20 each year:

SY 1381 = 21 March 2002 – 20 March 2003

SY 1382 = 21 March 2003 – 19 March 2004

SY 1383 = 20 March 2004 – 20 March 2005

1 Executive Summary

A review was carried out of the Afghanistan Reconstruction Trust Fund (ARTF) during January-February 2004. Main findings and recommendations follow.

The ARTF and Its Management

The ARTF has been the donor community's response to the national authorities' strong and consistent request for a single, predictable, accountable source of un-tied funding for the recurrent budget, which is the Government's top priority.

The ARTF has successfully mobilized the necessary resources from a wide range of donors. This has allowed the GOA to continuously provide the key public services across the country. The policy of permitting donor preferences where funding gaps exist ensures continued donor support for the ARTF. However, the danger that such preferences may in the future create constraints/rigidities for allocating funds needs to be monitored.

The Bank is taking its responsibilities as Administrator of the ARTF seriously. A management team has been established to assist GOA implement and monitor activities, and a financial and disbursement team assists the correct and timely utilization of funds. This is credited by the Bank to have improved the quality of financial reporting and monitoring, and has helped GOA accelerate implementation and disbursements considerably over the last year.

The Governance structure is seen as comprehensive yet flexible. MC members experience the MC meetings as increasingly important with discussions leading to several project proposals being rejected or modified. Minutes from the MC meetings have so far not been distributed outside the MC itself, however.

The donors meetings are seen as helpful, but too focused on administrative and financial detail and without policy content. Reporting is seen as comprehensive, accessible (web-site), though donors would like more issues and results orientation. Donors currently sense some lack of direction and dynamism in the Fund, which it is acknowledged is in part due to the recent change in Government.

The principle of having an independent Monitoring Agent is seen as positive, and the Bank has carried out an internal review of the MA's performance.

The ARTF is seen to be in line with "best practice" principles for structuring and managing trust funds in post-conflict situations. It is also in accordance with the Paris Declaration's "good partnership principles" regarding Ownership, Alignment, Harmonization and Mutual Accountability for donor funding.

The ARTF Recurrent Window

Afghanistan has put in place most elements of a comprehensive public finance management (PFM) system, and is now working to both increase own revenue and maintain fiscal restraint.

The MA has supported the development of the PFM by demanding compliance with fiduciary standards, adjusting these standards to the realities of the country, and training public officials in implementing them. During the first phase, the MA focused on enforcement of general standards and was criticized as too rigid in applying them. Subsequent work focused on verifying the payroll – where problems so far identified

are seen as relatively minor – and lately has focused on O&M. While ineligibility was on average around 80% last fiscal year, it fell to just over 2% during the third quarter of SY 1383. This rapid improvement is due to MA and MOF training, information dissemination and performance monitoring, but even more to MOF reducing ministry allotments equivalent to ineligible expenditures submitted in the previous period.

Both Efficiency and Effectiveness of the Recurrent Window are seen as very good, not least of all because funding is provided on-budget and thus contributing to improved PFM, transparency and accountability.

The Relevance is seen as high and will remain so as the funding gap over the coming period will remain high. Impact is seen primarily in PFM improvements, but also in terms of public service delivery in key areas like health, education, basic infrastructure. Achievements are fragile, however, dependent on external technical assistance (TA) and continued improvement in national stability and security.

The institutional arrangements are transparent and flexible, reporting is good and accessible through innovative use of the Internet. But continued donor funding for the recurrent budget is dependent on GOA being successful in mobilizing own resources and showing a strong political commitment to achieving financial sustainability over a reasonable time horizon.

The operations of the Recurrent Window and of the MA are providing some capacity development, but this is largely *ad hoc* and not based on a longer-term CD strategy.

The ARTF Investment Window

The ARTF project portfolio includes activities in three areas: infrastructure, public sector CD, and community development. Commitments stand at around USD 150 million, with about one third has so far been disbursed.

As far as prioritization among the three kinds of projects, most agree that grant funds should not be used for capital intensive infrastructure projects, since most can find concessional loan funding, can generate service income or other forms of burden-sharing funding. Grants monies should instead focus on public goods and poverty reduction activities: community development and public sector CD.

Disbursements have grown slowly but recently increased rapidly, largely as early build-up of CD has led to greater absorption capacity by the projects (NSP, MISFA in particular). Performance and financial reporting started late and are not consistent. However, ARTF management has been active in monitoring projects in coordination both with World Bank task managers and project management (GOA and external).

From an efficiency viewpoint, most projects have high overhead costs due to the use of external managers/contractors for implementation. Projects in the infrastructure and community development groups have been more effective than the CD projects.

As GOA begins to move from a post-conflict to a development agenda, clear phase-out plans for all external management units should be elaborated. Phase-out plans should be in coordination with a capacity building plan.

The ARTF has so far not developed a gender policy. While a number of projects have gender targets, overall this is *ad hoc* and dependent on individual task managers rather than systematic policy.

CD in the Investment window has been designed and implemented at project level. The challenge is to raise the CD efforts to a programmatic or national level while assuring GOA's ownership and the sustainability of these investments.

Looking Ahead

The recurrent cost challenge may remain longer than is currently foreseen, since the government will be facing major challenges on both the revenue raising and fiscal restraint sides. The donors need to be realistic about this and forward looking in terms of providing required untied funding for this.

The Recurrent Window is *de facto* budget support, but there is no permanent forum where the policy issues surrounding budget support can be addressed.

The Investment Window should focus on activities where untied pooled funds contribute the most to reducing overall transaction costs, and also identify areas where synergies can be established with the concerns of the recurrent window, namely weaknesses in PFM capacity.

Afghanistan is putting in place a reasonably transparent and competitive public service salary scale for skilled labor, in part using ARTF funds both for the PRR and public sector CD projects. This is a major achievement in the context of general public sector reform. But these efforts are suffering from donor funding distorting the market for skilled labor, ratcheting up wages and attracting away from the national public and private sectors many of the best skilled nationals.

The key imbalance in this market is due to poor supply of more and better skills. The efforts so far are uncoordinated, expensive, and without clear choices regarding the balance between on-the-job skills upgrading versus formal qualifications training, what training should be provided within-ministry and what should be procured from external institutions, whether the public sector should establish a public administration institute or rely exclusively on universities and other schooling institutions, etc.

TA today is costly, usually not provided based on open competition, the contracts are not owned by GOA and there is thus little performance management and control. Considerable savings can be generated through better structuring and procurement of TA.

As Afghanistan's public sector planning and budgeting becomes more medium-term and comprehensive, the difference between recurrent and investment activities becomes less important. As the country's PRS comes into place, more donors will be willing to provide general budget support directly to the Treasury. However, this point is still some years off.

Recommendations

1. The ARTF structure and procedures should be maintained – they appear functional and in line with "best practice" as it is considered today.
2. *Reporting* should be modified: (i) MC minutes should be distributed to ensure full insight into ARTF decisions; (ii) reports should highlight results, issues, changes to put focus on the dynamics and net contributions of the ARTF, put the ARTF into perspective, and stimulate debate and interest around the considerable achievements of the ARTF.

3. A GOA-led Policy Forum should be established to develop a more permanent policy dialogue alongside the ARTF. The scope/agenda and participation in the Forum needs to be decided among the parties.
4. The structure and priority of the Recurrent Window should be maintained. The World Bank in close collaboration with the national authorities should continue to encourage the donors to provide untied funding for the budget through the ARTF as the most efficient and effective support modality.
5. The use of a Monitoring Agent has proven to be highly valuable and should be continued.
6. The Investment Window should pay particular attention over the coming period to PFM capacity building (CD), including GOA-managed TA procurement. This will generate synergies with the Recurrent Window while addressing the area where donor-funded activities generate the highest transaction costs, namely TA and capacity building. It will strengthen PFM and thus create conditions for untied budget support.
7. The ARTF should be conceived of as passing through different phases: (i) the Emergency Phase, just ended, (ii) PFM-CD and TA management for the next five years or so, (iii) PRS funding phase once a credible PRS is in place (at which time the distinction between Recurrent and Investment Windows will largely be illusory), (iv) Budget Support Transition. As the conditions for direct budget support develop, the value-added of a donor-managed coordination mechanism like the ARTF will diminish. But for the time being, it provides important services for a number of donors, and as long as this is the case, it should be maintained, till a final sunset date is agreed to by the parties.

2 Introduction

The Afghanistan Reconstruction Trust Fund (ARTF), a multi-donor trust fund administered by the World Bank, has since mid-2002 funded the Government of Afghanistan's (GOA) recurrent budget, but is also increasingly used as a mechanism to fund priority investments in GOA's National Priority Programs (NPPs). These are based on the National Development Framework (NDF). The ARTF Program thus contains two components or "windows":

- Funding for recurrent costs of the budget (salaries of civil servants plus operations and maintenance, O&M): "Recurrent Window"
- Development Projects: "Investment Window".

2.1 ARTF Objectives

The ARTF provides a mechanism for coordinated funding of reconstruction activities in line with agreed priorities of the Government. The ARTF is designed to:

- (i) promote transparency and accountability of reconstruction assistance;
- (ii) help reinforce the national budget as the vehicle for promoting alignment of the reconstruction program with national objectives;
- (iii) reduce the burden on limited government capacity for the first few years of re-engagement, while promoting capacity building over time;
- (iv) help fund the essential recurrent budgetary expenditures required for the government to function effectively; and
- (v) provide a convenient mechanism for donors to fund priority investments.

2.2 Objectives of the Study

The World Bank acts as Administrator of the ARTF. As such, it commissioned an evaluation of the ARTF. The objective was to assess the effectiveness and impact of ARTF operations over the past two and a half years (March 2002 – end 2004). The assessment was to be made in terms of *relevance, impact, effectiveness, efficiency, responsiveness, and the sustainable benefits of the ARTF's activities, and overall institutional arrangements*. The full Terms of Reference are given in Annex A.

2.3 Methodology

The evaluation began with a document review in January (Annex C). Interviews were then carried out with donor head office representatives. This included a visit to the US in mid-January 2005, to interview staff from the World Bank, IMF and US Treasury in Washington, and staff from the UN system in New York. Other donor officials were either interviewed in person or by telephone, based on a Conversation Guide that had been forwarded beforehand (Annex D).

A team organized a two day workshop in Oslo January 27-28 where the Inception Report, the Conversation Guide for the field work (Annex E) and the planning for field work were finalized.

During the field work February 12-25, most of the time was spent in Kabul interviewing GOA officials, donor representatives, project staff, technical assistance personnel, and other informants (see Annex B). The team spent two days outside the capital visiting provincial administrations and community development projects.

2.4 Structure of Report

This Report contains four substantive chapters:

- Chapter 3 is an overview of the ARTF, the management of the fund, and how it compares to "lessons learned" about trust funds and aid coordination.
- Chapter 4 reviews the Recurrent Cost window and assesses its performance;
- Chapter 5 presents the projects that are funded and the achievements to date;
- Chapter 6 looks ahead, assessing options for the future.

These four chapters contain a section on Conclusions and Recommendations that make up the Executive Summary. In addition are a number of annexes:

- Annex A: Complete *Terms of Reference* for the Evaluation Mission;
- Annex B: List of Informants;
- Annex C: Documents Consulted;
- Annex D: Conversation Guide for donor head office officials;
- Annex E: Conversation Guide for the field work in Afghanistan;
- Annex F: Process for submitting projects to the ARTF for funding;

2.5 Review Team, Acknowledgements and Disclaimer

The evaluation was carried out by Mr. Arne Disch (team leader) and Ms. Riselia Bezerra of Scanteam/Norway, Mr. Martin Greeley, Institute of Development Studies, University of Sussex/UK, and Mr. Kjeld Elkjaer, CD Consultants/Denmark.

The team received full support from all GOA, donor, and NGO offices approached and communities and projects visited, for which we would like to express our sincere thanks. The openness and generosity shown was much appreciated. A special Thanks goes to the World Bank staff in Washington and Kabul, who went out of their way to support and facilitate the work of the team, for which we are grateful.

This report and its findings are the sole responsibility of the evaluation team, and do not necessarily reflect the views of the Afghan authorities, the World Bank or any other donors or funding agencies engaged with the ARTF.

3 The ARTF

This section reviews the history of the ARTF, the funding that has been provided and disbursement levels as at end 2004. The management structure of the ARTF is presented, before it is assessed against "lessons learned" regarding trust funds, and "best practice" approaches to aid coordination. The Bank's performance as ARTF administrator is then looked at before the Conclusions and Recommendations.

3.1 Background to the ARTF

Once the international community intervened in Afghanistan to oust the Taliban regime in the fall of 2001, it was clear that large-scale assistance would be urgently required. This was both to address the physical damage and the many years of neglect that the country had suffered, but also to ensure support for a regime that would bring stability, control and socio-economic development to Afghanistan.

A first donors' conference took place in Islamabad at the end of November 2001. Following this, it was agreed that the needs of the interim authority that was to be established early 2002 should be met by a UNDP-administered Emergency Trust Fund. This was due to the UN being in charge of the political transition, as well as having a large operational system on the ground because of its support to civil society actors during the Taliban period. In line with the political transition timetable set out at Bonn in December 2001, the UNDP Trust Fund was to expire after six months with the convening of an emergency *Loya Jirga*. The *Loya Jirga* was to establish a two-year transitional government, before full elections were to be held by the end of 2004. Donor meetings early 2002 in Brussels and Tokyo endorsed the notion of the Afghanistan Reconstruction Trust Fund (ARTF) to succeed the UNDP fund.

The World Bank Board had discussed a draft Bank assistance strategy to Afghanistan, including the concept of the ARTF as a multi-donor trust fund. The model was trust funds that had been established in other post-conflict situations, such as in the Palestinian Territories (the "Holst Fund"), Bosnia-Herzegovina, and East Timor.

The ARTF was approved by the World Bank Board on 27 March 2002. The Grant Agreement was signed in May, and the Fund began operating in late May 2002. The ARTF was set up with the intention of providing support only for the initial years, during which GOA would establish the capacity to mobilize revenue to cover its recurrent budget. The ARTF closing date was first established for two years after the election of a permanent government or June 30, 2006, whichever came first. In June 2004, however, donors agreed to extend the validity of ARTF from June 2006 to end June 2010, which is now the foreseen closing date.

3.2 ARTF Funding

By early 2005, 24 donors have pledged nearly USD 1 billion to the ARTF since its inception. The *share* of each donor's funding to Afghanistan that goes through the ARTF varies considerably, but for some of the larger donors it represents a significant proportion.

As of 18 February 2005, the amount committed to the Recurrent Window was USD 603 million, of which USD 469 million had been disbursed (plus an initial advance of

USD 50 million in the Special Account) (Table 3.1)¹. There are nine active projects funded by the Investment Window with combined commitments of USD 101 million, of which nearly USD 47 million have been disbursed². While disbursements under the Investment Window have been fairly slow till recently, the activity levels have increased substantially towards the end of 2004 and early 2005, pointing to an acceleration in funds disbursements.

In December 2004 the Management Committee approved four projects for funding: (i) USD 20 million for co-financing the rehabilitation of the Naghlu hydropower plant; (ii) USD 20 million for an Urban Water Supply and Sanitation Program; (iii) USD 3.8 million for technical assistance to implement the Kabul Urban Reconstruction Project, and (iv) USD 3 million for the Lateral Entry Program (LEP).

Table 3.1: ARTF Financial Status, as of January 2005 (in USD million)

TF Name	Signed	Effective	Closing	Commitment	Disbursed
Recurrent Expenditure	5/13/02	5/13/02	6/30/10	521.00	519.67
Active Investment Projects:					
TA & Feasibility Studies Facility	3/8/03	3/8/03	9/30/05	14.00	5.65
Afghan Expatriate Program				5.00	0.00
NEEP	3/14/03	3/14/03	9/30/05	16.62	8.31
Microfinance Project (1)	7/10/03	7/10/03	6/30/06	17.00	12.15
Telecommunications	7/10/03	7/10/03	12/31/05	6.13	0.66
Kabul Roads	11/8/03	2/17/04	6/30/05	3.00	2.07
Power Supply To Kabul	12/10/03	2/2/04	6/30/06	7.44	2.61
CCFO	10/11/03	11/19/03	2/28/06	5.10	2.05
National Solidarity Program	9/30/04	9/30/04	6/30/06	27.00	13.21
			Subtotal	101.29	46.70
Closed Investment projects :					
UNDP Police 1, 2 & 3 (LOTFA)				21.64	21.64
			Total investment projects	122.92	68.34

Source: Afghanistan Country Portfolio Status Report, January 2005. World Bank, Kabul office.

1: This includes the initial USD 1 million to the Microfinance Fund.

¹ This report has not included the various tables over donor contributions, etc, since these are reported on a regular basis through the World Bank web-site: www.worldbank.org.af. On the right hand bottom corner, there is a link to the ARTF, where the full quarterly reports to the donors as well as the latest monthly financial report are presented. In the most recent report, of 18 February 2005, table 2 shows actual and expected donor contributions by donor by year.

² As will be seen from the table, the so-called UNDP Police Projects, or Law and Order Trust Fund for Afghanistan (LOTFA), are included here. These projects have a different status from the rest as the ARTF functioned only as a "pass through" mechanism for this funding. The reason is that the Bank is prohibited by its rules from providing funding for security-related activities, and as Administrator of the ARTF could therefore not become directly engaged in managing this component. Instead, UNDP is the manager of LOTFA, and has the fiduciary and results responsibility.

The ARTF does not permit ear-marking of funds for particular activities by the donors (this is a World Bank policy for all trust funds that it manages). However, donors can express preferences for specific projects or programs for a portion of their overall contribution. These preferences can be expressed only for activities for which a funding gap exists. This helps donors show their constituencies that funding is going to areas that have been designated as priority areas by their political decision makers back home. A total of USD 79 million out of the USD 429 million pledged in SY 1383 came with such preferences, compared with only USD 16 million in SY 1382³. As long as the funding gap provision remains, this increase in preference noting is not a problem, but if donors begin *de facto* ear-marking, this may create some constraints for future management of the ARTF which needs to be considered.

3.3 Governance Structure

The size of funds made available, the large number of donors involved, and the political importance attached to the success of donor support to Afghanistan, has meant that the governance of the ARTF has been paid particular attention. The oversight and reporting structures and practices are thus quite comprehensive.

3.3.1 ARTF Administrator

The World Bank is the Administrator of the fund. As such, it has assumed the responsibility of monitoring Fund performance, and in particular to assure that funds are disbursed in accordance with acceptable fiduciary standards (Recurrent Window) and to priority activities (Investment Window) in line with policies set by GOA and agreed to by the donors.

Start-up of projects and disbursements were to begin with a problem, as the Afghani authorities had to prepare the national policies, re-constitute the public sector, recruit qualified staff, etc, while at the same time attending to the pressing needs of rehabilitation and reconstruction. As the bottlenecks became more apparent, the Bank as of early 2004 established an ARTF management team in its Kabul office, which currently consists of three persons. The ARTF Manager reports both to the Bank's Country Director for Afghanistan in Washington, and the Bank's Country Manager in Kabul. The management team is responsible for the day-to-day monitoring of the Fund's performance, including keeping in touch with the Ministry of Finance (MOF) for overall Fund issues and the Recurrent Window in particular, as well as tracking the various projects' progress. The team is responsible for reporting back to the stakeholders, which is done through its web-site (see footnote 1), quarterly donor reports and newsletters, and informal correspondence and reports.

The Bank has furthermore put in place a financial management and disbursement team, to look after both regular World Bank IDA credits, and the ARTF. This team meets regularly with Afghani officials, carries out trouble-shooting, and trains GOA officials in Bank procedures.

3.3.2 Management Committee (MC)

The ARTF is overseen by a Management Committee (MC) consisting of representatives from the Asian Development Bank (ADB), the Islamic Development

³ The Administrator's report (see footnote 1) includes table 3 that shows current preferences by donor by project, by year pledged and amount paid in.

Bank (IDB), the United Nations Development Programme (UNDP), and the World Bank. The MC is responsible for reviewing progress and taking key decisions, including the approval of investment projects proposed for ARTF financing. The MC meets on an "as needed" basis, which has been on average every other month during the last two years. The World Bank acts as a secretariat to the MC, preparing the documentation for the meetings as well as preparing the minutes afterwards. These minutes have so far only been distributed to the MC members themselves.

The establishment of an MC with participation by other leading multilateral actors is an innovation of the ARTF, as normally the World Bank would assume the full managerial of other trust funds. The MC system seems to work well, with members expressing satisfaction at the voice being provided and the collegiality of the meetings. As more projects come before the MC, the policy dimensions and principles that should underpin choices have become more explicit and led to more contents-based discussions within the MC, which members see as a positive development.

3.3.3 Steering Committee/Donors Committee

A Steering Committee consists of the MC members, all donors that provide at least USD 5 million in contributions per year, plus an additional two seats for the smaller donors where these two seats are voted in on a rotational basis. The Steering Committee (or Donors' Meeting, which it is more informally referred to), generally meets on a quarterly basis. These meetings have so far largely focused on administrative and performance matters regarding the ARTF. The last such meeting took place on 8 February 2005.

While the meetings are seen as an important forum for updating the donors on the status of activities, a number of donors expressed an interest in more issues-focused meetings that could address the framework problems the ARTF is facing.

3.3.4 Monitoring Agent

The GOA receives ARTF funds under the Recurrent Window as reimbursements of eligible expenditures. The Bank has contracted an external Monitoring Agent (MA) who monitors, supports and reports on these claims against eligibility criteria and fiduciary standards (see Box 2).

The MA is to (i) provide timely reviews and transmission of withdrawal applications to the World Bank; (ii) screen GOA withdrawal applications and related documentation to ensure expenditures submitted for reimbursement under ARTF are consistent with the grant agreement and related eligibility criteria; (iii) review operations of the ARTF special accounts; (iv) monitor expenditures of the ARTF to ensure that funds are disbursed for the purposes provided; (v) work closely with MOF and other agencies to ensure that the rules for eligibility of expenditure are widely understood; (vi) monitor the progress of GOA in complying with fiduciary benchmarks, and contribute to their continuous improvement; (vii) maintain the civil service headcount database at MOF; (viii) improve capacity of the central, provincial, and district government staff in financial management and accountability of recurrent expenditures; and (ix) review reporting from MOF and ministries receiving ARTF, and bring critical issues to the early attention of the WB and Government.

The MA focused early on on the central MOF procedures, then moved on to assessing performance in the relevant line ministries, and is now also carrying out site visits to provinces, including line ministry departments there.

3.3.5 Project Proposals

All proposals for activities that are to receive ARTF funding come from the MOF. These can in principle come from any line ministry in the Government, but must be accompanied by a justification in terms of its importance to GOA's NDF and NPPs (see Annex F for the project proposal procedures).

3.4 The ARTF as Trust Fund

In a recent study on the World Bank's experience with trust funds for post-conflict situations, the Executive Summary begins by noting that "Post-conflict reconstruction is first and foremost an institutional challenge. Hence, the first lesson of experience for aid in post-conflict situations is the imperative of assuring robust linkages between the aid and the rebuilding of local institutions, and the core challenge is the balancing of immediate reconstruction priorities with long-term institutional development" (Schiavo-Campo, p. i). The study looks at four examples – Bosnia-Herzegovina, the Palestinian Territories, East Timor, and Afghanistan – and notes that while there are some similarities amongst the cases, the most important lesson is that such funds need to address the specific issues facing that country: "In Afghanistan, the key objective is to reconstitute a functionally limited but effective state, and to reduce economic distance by re-establishing security and restoring transportation and communication links" (op. cit., p. i).

More specific lessons learned concern design and procedural issues. The Fund must fulfill both a fiduciary (legal, accounting, disbursement, reporting) and executive function, where the latter includes agreed reconstruction program and transparency in implementation. It is important to avoid a fragmentation of funding vehicles between the recurrent and investment budgets, and it is also imperative to have in place measures to minimize corruption and leakages *before* fund commitments are made. Finally, the paper claims that it is important that the government and donors agree from the outset on an exit strategy for the aid management agency.

Chapter 4 looks at how and to what extent the Recurrent Window in fact is contributing to the institutional development of the country, as well as the degree to which fiduciary standards have been followed and anti-corruption measures put in place.

While the ARTF is a vehicle for both recurrent and investment costs, the share of investment funding that goes through the ARTF is minuscule. In SY 1383, which ended 20 March 2005, the ARTF disbursed about USD 40 million, while it is estimated that more than USD 3 billion went into various investment activities during the same period. The ARTF thus provided a little over one percent of total investment funds.

The link between the investment and recurrent windows are discussed more in the last chapter, however, as there are some possibilities for making the limited investment funds more strategic and better linked with the recurrent budget support. Furthermore, as noted above, there is already an agreement on the "sunset date" for the ARTF, but this is an issue that is also returned to in the last chapter.

3.5 Aid Coordination

Over the last several years, the international community has spent considerable time trying to improve efficiency and effectiveness of aid. In the Monterrey Consensus

(March 2002), developing countries committed themselves to policies and institutions that stimulate growth, reduce poverty and contribute to achieving the Millennium Development Goals (MDGs), while the donor countries were to provide more and better aid and improve trade and debt policies.

A year later, the Rome Declaration (February 2003) underlined the need for donors to align development assistance with partner country strategies, harmonize policies and procedures, and implement principles of good practice in development cooperation. In Marrakech (February 2004), agreement was reached on a global partnership that would focus on managing for results.

The recently concluded High Level Forum in Paris (28 February-2 March 2005) summarized the agreements so far through the so-called "Paris Declaration on Aid Effectiveness". Key to the Declaration are the Partnership Commitments, where the key dimensions are *Ownership* by the host country of the overarching development plans that are being funded, *Alignment* between donors' and partners' priorities, *Harmonization* amongst donors regarding rules and procedures used, and that the actors jointly will be *Managing for results*. Finally, there must be *Accountability* by both parties for successful partnership. In order to track performance along these dimensions, 12 indicators of progress have been agreed to (see Box 1 below).

The ARTF is in many areas in line with the Paris Declaration's understanding of "best practice" approaches. It is providing support to the general budget and priority investment activities, and therefore is in accordance with the Alignment principle. Because it is a trust fund with a transparent and acceptable set of procedures for disbursing and overseeing the resources, it is encouraging the Harmonization between a large number of donors regarding their support to the GOA. Since funding only goes to public sector activities that have been defined in GOA's budget, the National Development Framework and its resultant National Priority Programs, the ARTF is hence also ensuring that GOA Ownership is in place. Through the constant publishing and updating of financial and performance information, it is respecting the Mutual Accountability principle. The greatest weakness is in Results management on the projects side, as discussed in chapter 5.

However, the main point is that the ARTF Recurrent Window has been a response to the Government's strong, systematic and continuous request to the donor community to put its resources together into the ARTF. GOA has wanted a single, predictable, accountable source of funding that would ensure mobilization of sufficient funds for the recurrent budget. It needed to provide key public services on a continuous basis in those areas where the population can see and benefit from them, such as basic health, education, and infrastructure. These are largely recurrent cost intensive and thus require continued and large-scale un-tied funding. The ARTF has been able to deliver this, and for this the Government has expressed its great appreciation – to the Bank as Administrator, coordinator and co-sponsor of fund mobilization activities; to the MC members for taking on their management and coordination functions; and to the donors for continuously responding to the requests for resources.

Box 1: Indicators of Progress

The indicators are to be measured at country level, while the overall objectives look at aggregates at international level by the year 2010. While the first indicator is that partners have an operational PRS, the objective is that 75% of partner countries have this by 2010.

A. Ownership

1. *Partner has operational development strategies* with clear strategic priorities, linked to a medium term expenditure framework and reflected in annual budgets.

B. Alignment

2. *Reliable country systems*: Public financial management and procurement that adhere to acceptable good practices, or have a reform program in place for these.
3. *Aid flows aligned on national priorities*: Percent of aid reported in national budget.
4. *Strengthen capacity by coordinated support*: Percent of donor CD support provided through coordinated programs.
5. *Use of country systems*: Percent of aid flows that use partner country procurement or PFM systems.
6. *Avoiding parallel structures*: Number of Project Implementation Units (PIUs) per country.
7. *Predictability*: Percent of aid disbursements released according to agreed schedules in annual or multi-annual frameworks.
8. *Aid is untied*: Percent of bilateral aid that is untied.

C. Harmonization

9. *Use of common arrangements and procedures*: Percent of aid provided as SWAPs.
10. *Shared analyses*: Percent of joint field missions and/or country analytic work that is joint.

D. Managing for Results

11. *Results oriented frameworks*: Existence of transparent and monitorable performance assessment frameworks to assess progress against national development strategies and sector programs.

E. Mutual Accountability

12. *Mutual accountability*: Degree to which there are periodic assessments of mutual performance between donors and partners.

3.6 Conclusions and Recommendations

The main *Findings* and *Conclusions* are the following:

- The ARTF has been the donor community's response to the national authorities' strong and consistent request for a single, predictable, accountable source of untied funding for the recurrent budget, which is the Government's top priority.
- The ARTF has successfully mobilized the necessary resources from a wide range of donors. This has allowed the GOA to continuously provide the key public services across the country (see chapter 4 on this).
- The policy of permitting donor preferences where funding gaps exist ensures continued donor support for the ARTF. However, the danger that such preferences may in the future create constraints/rigidities for allocating funding needs to be monitored.

- The Bank is taking its responsibilities as Administrator of the ARTF seriously. A management team has been established to assist GOA implement and monitor activities and a financial and disbursement team assists the correct and timely utilization of funds. This is credited by the Bank to have improved the quality of financial reporting and monitoring, and has helped GOA accelerate implementation and disbursements considerably over the last year.
- The Governance structure is seen as comprehensive yet flexible.
- The MC members experience the meetings as increasingly important with discussions leading to several project proposals being rejected or modified. Minutes from the MC meetings have so far not been distributed outside the MC itself, however.
- The donors meetings are seen as helpful, but too focused on administrative and financial detail and without policy content. Reporting is seen as comprehensive, accessible (web-site), though donors would like more issues and results orientation (chapter 5). Donors currently sense some lack of direction and dynamism in the Fund, which it is acknowledged is in part due to the recent change in Government.
- The principle of having an independent Monitoring Agent is seen as positive, and the Bank has carried out an internal review of its performance (chapter 4).
- The ARTF is seen to be in line with "best practice" principles for structuring and managing trust funds in such post-conflict situations.
- The ARTF is also seen to be in accordance with "good partnership principles" regarding Ownership, Alignment, Harmonization and Mutual Accountability for donor funding.

Based on the above, the Evaluation Team's ***Recommendations*** are:

- The ARTF structure and procedures should be maintained – they appear functional and in line with "best practice" as it is considered today.
- *Reporting* should be modified: (i) MC minutes should be distributed to ensure full insight into ARTF decisions; (ii) reports should highlight results, issues, changes to put focus on the dynamics and net contributions of the ARTF, put the ARTF into perspective, and stimulate debate and interest around the considerable achievements of the ARTF (see following chapters).

4 Support to the Recurrent Budget

Over the previous 20 years, public administration including public finance management (PFM) suffered a fairly continuous deterioration. Since the installation of the interim administration at the end of 2001 (SY 1380), considerable attention has been paid to putting in place a more modern PFM system, covering planning and budgeting, accounting, audit and external accountability. This has been done while also strengthening overall transparency by making much of key PFM information publicly available through the Internet⁴.

While the systems and performance have improved quite rapidly, this has been done with heavy use of external Technical Assistance (TA). This makes the gains to date vulnerable to continued TA presence. This vulnerability is not made less by the fact that today there are at least five different consultancy groups working in the Ministry of Finance under separate contracts funded by four different donors.

4.1 ARTF and the GOA Budget.

Afghanistan has traditionally had a highly centralized public administration, with key decisions taken and resources controlled by Kabul. In the provinces, the *mustoufiats* handle the payments and revenue collection. Since most of the ARTF financing is paying for the recurrent costs of the government, where most services are in fact provided at the provincial and district levels, the *mustoufiat* plays a key role in ensuring that ARTF funds are properly applied and accounted for.

Investment projects are largely handled at central ministry level. Lack of capacity to develop projects, prioritize the investments, and track performance of on-going activities remains one of the weak parts of GOA's overall PFM efforts.

The GOA distinguishes between its Core Budget, which consists of the funds that go through the Treasury account and over which it therefore has full control, and the External Budget. External Budget funds flow outside the GOA's accounts, such as where a donor provides funding to a UN agency, NGO or private contractors for implementation of projects. These funds are used to finance projects within the National Development Budget, and discussions take place between the parties as part of the general budget process.

For SY 1383, it is estimated that the total budget was about USD 5.1 billion. Of this, donor funding made up USD 4.8 billion. Only USD 1.7 billion was core budget – meaning it was implemented by GOA – but of this, USD 1.3 billion was under direct donor supervision and fiduciary oversight (World Bank 2005, p. 7). This latter category include ARTF funding, because while the ARTF funds go through GOA systems, the MA is providing the oversight function. So while two thirds of expenditures are completely outside GOA's control, only about 8% of public funds were fully GOA's responsibility – a difficult situation to be in.

⁴ The World Bank just carried out a Public Finance Management System assessment that describes the system, current performance and foreseen improvements. The draft of this report is being distributed in connection with the Afghanistan Development Forum. Rather than replicate parts of the information and analysis in that very comprehensive and up-to-date document, this report assumes interested readers will have read the Bank's PFM report (see World Bank 2005).

As can be seen in table 4.1, the ARTF has covered a significant share of the non-security recurrent budget. Most of the funding has gone for personnel expenditures, which in practice means the donors have ensured that the labor intensive public services – health and education – have been made available to the population.

Table 4.1: National budget, and ARTF contributions (in AFA millions)

	SY 1381	SY 1382	SY 1383 (budget)
Wages (non-security)	3,258.8	6,682.5	9,448.3
O & M exp (non-sec'y)	2,334.8	4,466.5	9,644.2
Total Recurrent (non-security)	5,593.6	11,149.0	19,092.5
ARTF contribution	2,686.7	9,643.2	(committed) 12,103.2
ARTF, % recurrent non-security	55%	86.5%	63.4%

4.1.1 Revenue

Afghanistan revenue collection during the years of upheaval was insignificant. The new authorities have therefore put a lot of effort into re-establishing a more solid footing for public finances. Over the past three years, total revenue collected has increased from AFA 5.8 billion in SY 1381 to AFA 10.4 billion in SY 1382 and an expected AFA 13.1 billion (about USD 280 million) in SY 1383. The target is to reach AFA 75 billion (approximately USD 1.5 bill.) by SY 1390, thereby largely covering expected operating costs.

Table 4.2 Total Revenue SY 1380-1382, by category:

	Customs	Taxes	Sales	Fees	Rents	Land tax	Miscellaneous	TOTAL 1380-82
AFA (mill.)	7,675.3	1,511.3	2,718.1	3,455.4	1,210.5	1.4	458.4	17,030.4
USD (mill.)	159.9	31.5	56.6	72.0	25.2	0.0	9.6	354.8

A draft action plan for increased revenue collection is presently being discussed in the MOF. The plan intends to improve total revenue collected by maximizing the revenue possible from existing sources, eliminate or minimize leakages, and identify and develop new sources. The paper believes that it is feasible to meet the revenue forecast laid out in the previous government's strategy paper, "*Securing Afghanistan's Future*" (SAF), and if conditions are right, to achieve this within a shorter time span than foreseen in the SAF.

An important feature is the planned amendment to the customs and revenue codes, giving customs and revenue officers enforcement powers. This is to include seizure of property, temporary closure of business, liability of managers, restrictions on transfer of ownership of property, etc. in cases of unpaid taxes.

A central concern is simply to go more aggressively after revenue that MOF *knows* is due. In one border city, 24 known importers currently owe the tax authorities USD 4 million – nearly 1.5% of SY 1383 expected revenue income. Another issue is that while MOF estimates that there are around 100,000 who earn more than AFA 150,000

– the cut-off point above which income tax is due – less than one percent of these actually pay income tax.

As part of the reforms, MOF now demands that all revenue collected by the provinces is transmitted to Kabul. Previously a number of provinces' followed what was termed the "net flow" approach, whereby they would retain for own expenditures what they had been allocated over the budget. Now all provincial revenues are transferred to Da Afghanistan Bank (DAB – the Central Bank) to a revenue account over which only Treasury in MOF has authority to spend. In return, based on approved budgets for the individual provinces, DAB transfers are made directly to the provincial accounts on a monthly basis.

Box 2: Increasing Afghanistan's Revenue

The activities envisaged in the MOF revenue paper are divided into three main areas:

1. **Legislative:** New revenue law (concentrating on large tax-payers) and new customs code which among other things are to provide revenue and customs officers with enforcement powers, strengthen the legal basis for aggressively pursuing delinquent tax-payers, and in general make Afghanistan's legal code in line with international best practice in terms of ability to identify and collect public revenue.
2. **Corporate tax reform:** This is to ensure that the private sector pays the taxes and fees that are common in other countries. The new tax will therefore include non-deductibility of dividends, royalties and fees; Tax on interests, royalties and management fees; Branch profit tax; Limit on deductible interest; Limited deductibility of admin. Costs to associated entities; Transfer pricing; Quarantining foreign losses against foreign income (foreign companies branches); Clarify the basis for accounting; Modernize corporate tax measures for extractive industries; Introduce accelerated depreciation instead of tax holidays; Provide correct treatment of pre-production costs; and other steps. These measures will be backed up by an effective and efficient revenue administration with a speeded up large taxpayer office, establishment of provincial revenue directorates. Revenue collection will be organized along business sector lines so that all businesses will be visited. Revenue officers are to be trained with a new curriculum being developed.
3. **Tax payer education:** MOF wants to produce a taxpayer's manual/guide book explaining why paying taxes is important, showing how tax funds are spent. MOF believes that the attitude among both tax-payers and tax collectors needs to be improved if the fiscus is going to have a realistic chance of collecting the revenue that is potentially available.

4.2 The Monitoring Agent (MA)

The MA provides monthly reports on the review and verification of eligible expenditures and the performance of related accounting, payroll, procurement and payment systems. The monthly reports are issues-focused, detailing the overall operations and provide aggregated and detailed financial information including expenditures reimbursed, the status of withdrawal applications in process, status of special accounts, eligible and ineligible expenditures to support month to month analysis.

More detailed quarterly reports provide analysis of trends in eligibility, expenditure execution problems and recommend corrective measures. The MA reports on progress made over the quarter in meeting the fiduciary benchmarks agreed between the MOF and ARTF. The MA meets regularly with the Bank and GOA to discuss issues and findings.

4.2.1 MA Activities

The ARTF supports the recurrent budget based on a reimbursement modality. Documentation for the expenditures GOA wants the ARTF to refund is forwarded to the Monitoring Agent for verification before it is then sent to the World Bank office for disbursement into GAO's account in DAB. This by-pass operation via the MA is what allows the ARTF to ensure that expenditures are in compliance with the criteria that have been agreed to (see Box 3 for the standards that are currently in force).

It may be helpful to distinguish three "phases" in the activities of the MA: (i) getting the system in place, (ii) verifying the payroll, and (iii) checking operations and maintenance (O&M) expenditures.

Early Compliance Concerns

During the first phase, the Monitoring Agent was sticking quite rigidly to the contract in terms of demanding full compliance with the reimbursement criteria and sending non-acceptable documentation in return to the MOF. MOF officials experienced the MA as inflexible and unhelpful during this period, as the MOF simply was getting documentation in return without advice regarding how problems could be addressed. This "do it by the books"-approach led to delays in reimbursement by the ARTF, which in turn created cash flow problems for the government. MOF officials claimed that reimbursement had been delayed up to two months on occasions, and that on at least four instances MOF had had to solve the cash flow problems by using other funds available to bridge the funding gap.

Two lessons were learned from this early phase. The first was that some of the compliance criteria, while corresponding to Afghani rules and regulations, were too rigid. The main issue was the time available for local administrations to provide the documentation for reimbursement. For many areas these deadlines just could not be met⁵.

The other was the need for MA to become pro-active and provide advice and suggestions in terms of how short-comings should be addressed. The MA has addressed this problem among other ways by producing a small hand-book, in Dari, that lays out the rules to be followed, and how this can be done. Along with the handbook, MA staff have provided some hands-on training, in part during site visits, in part during more formal sessions, to make financial management staff in the ministries and *mustoufiats* better equipped to carry out their tasks.

During this early phase, the MA also assisted the MOF in preparing the documentation for ARTF reimbursement. There was therefore a fair amount of "hand holding" done by the MA to help GOA officials comply with World Bank standards and regulations, so that the processing of the claims could run smoother.

The MA was therefore seen to begin with to be too rigid, causing disruptions in the flow of ARTF funds to government coffers. On the other hand, the MA helped MOF establish routines for more efficient processing of ARTF reimbursement claims, thus over time strengthening the overall performance of the reimbursement mechanism.

⁵ During the visit of this mission, team members were informed of schools that were two days' walk from the provincial capital – in a province that can be reached by car within about an hour from Kabul. In provinces that are heavily affected by snow, seasonal aggravation of poor roads means that it can literally take months for some officials to get to their provincial capital in winter.

The "Payroll Phase"

In addition to the desk verification of reimbursement documentation, the MA conducts on-site visits to ministries, and more recently also to provinces and districts. The key concern initially was payroll – to verify that the staffing lists forwarded to the ministries correspond to actual staffing in the field, that the people on the list exist and have been hired and thus eligible for payment, that there are no "ghost workers" or persons who occur on several lists, that the salary payments forwarded to the provinces in fact are paid out to the teachers and health staff, etc.

While this kind of payroll verification has begun, it is recognized that this is just the beginning of what needs to become a more careful scrutiny of payroll issues. At the same time, the MA has so far found that inaccuracies and problem listings are fewer than had originally been expected.

The key lesson has been, however, that these on-site visits are necessary and helpful. In part this is to ensure enforcement and compliance with standards and rules and making managers aware of the fact that inspections and verifications will take place at regular intervals and will become ever more rigorous. But the MA staff also experience that their visits are being seen as useful by field staff because of the training and more supportive approach that the MA is now taking in carrying out its task. While verification/accountability remains a key task, skills upgrading and improvement in performance through more support is also being included.

In large part due to the more active inspections, the delays in submission of payrolls have been reduced. At the same time, the time limits set for forwarding the documentation have been adjusted to the realities on the ground, providing a flexibility which is appreciated by the provinces. The result has been that ineligible payroll submissions from the provinces have been reduced to about 1%.

Box 3: ARTF Fiduciary Standards for Reimbursement

Fiduciary standards have been established for GOA expenditure to be eligible for ARTF reimbursement ("ARTF Fiduciary Standards", revised Dec. 2004). The standards have been divided into three groups:

1. Payroll:

- Only ministries which have submitted proposed employment limits can be reimbursed;
- Payrolls have to be submitted within three months after the end of the period in question (with certain possibilities for exemptions);
- Payrolls submitted with no allotted funds available are not reimbursable;
- Total payrolls have to stay within total cap of ministry's budget.

2. Operations and maintenance (O&M):

- O&M with no allotted funds available are not reimbursable;
- O&M expenditure is only eligible if documented within three months (HQ) and six months for provinces;
- O&M have to be in accordance with procurement instructions.

3. Cash management

- There are special detailed rules for travel and advances abroad
- Advances to provinces shall be settled within six months

More important, perhaps, is that the overall functioning of the payroll systems seem to be improving significantly. Payments from Kabul are made on schedule, and civil

servants in the provinces and districts are receiving their payments on a much more regular basis. There are still issues to be addressed, a typical one being that the security services often demand their payments first and any shortfall in funds received leads to teachers and health staff being short-changed. But the bottom line is that the payroll situation is considered to have improved dramatically over the last two years, and that further improvements are taking place. The contribution of the MA in helping this happen is acknowledged by most spoken with.

The "O&M Phase"

Once the payroll issue was seen as being addressed quite successfully, more attention was given to the problems of the operations and maintenance (O&M) reimbursement claims. During SY 1382, over 80% of O&M expenditures presented were returned as ineligible – a potentially disastrous situation.

During SY 1383, the O&M problems were addressed more aggressively. The MA and MOF identified the key problems, which had to do with poor understanding of the rules, poor implementation, and incorrect handling of some advances by the MOF. As a consequence, the MA and MOF have been providing a lot more information and skills upgrading regarding what kinds of expenditures are eligible under the ARTF rules for reimbursement; how to document the claims; what the timelines and standards are that need to be fulfilled. Perhaps more important is that MOF has informed the line ministries that if they present claims for reimbursement that are rejected by ARTF, MOF will deduct equivalent amounts from future ministry allotments. The reason for this policy was that for the ministries, whether the ARTF accepted their claims for reimbursement or not did not really matter – the MOF had already made the payments, so the reimbursement issue was seen as the MOF's problem. For the MOF the problem was very different: the non-reimbursement meant that the government was losing real resources. Since the ARTF funds were not being made available because of poor work by the line ministries, the MOF turned around and put the responsibility back on the line ministries.

Along with the MA's monitoring and assistance, this has worked wonders on the ministries' incentives to improve their compliance performance: ineligible O&M fell to 59% first quarter of SY 1383, to just over 20% during the second quarter, and for the first two months of the third quarter were down to an amazing 2.4% (see Administrator's Report to the donors for the period October-December 2004).

4.2.2 MA Role and Performance

The MA has played two different roles. On the one hand it has acted as an additional auditor/quality assessor by verifying expenditure reports, performed on-site visits to critically assess if documentation corresponds to reality, and has begun performance audits by looking into various aspects of the civil service payroll.

On the other, it has identified systemic problems and over time begun assisting the authorities in finding better solutions. One specific example concerns procurement rules. For lump-sum purchases over USD 250,000, Afghanistan now follows World Bank international competitive bidding rules. For purchases between USD 100,000 and USD 250,000, Afghanistan and the World Bank had slightly different rules. The MA suggested to the Bank that it adopt Afghanistan rules, since they were largely the same, but the slight differences were enough to cause irritation and delays. The Bank accepted the suggestion, and the MA in turn helped ensure that ministry officials were updated on what the formal procurement rules actually demand.

Over time, the MA has contributed to getting in place more realistic performance standards, is monitoring their performance but also assisting officials in understanding how they can perform better. Because the ARTF refunds such a high share of the total recurrent budget, the kinds of standards and performance that the MA demands for reimbursable expenditures is "spilling over" onto general budget management. For a number of government officials, the MA is thus seen to have taken on a more constructive role over time, and has provided major value-added to overall PFM performance.

4.3 External Audit

The audit of the GOA is performed by the Control and Audit Office (CAO). The only audit until now of the ARTF was done on the SY 1381 accounts, and forwarded by the CAO in March 2004. The audit for SY 1382 is expected shortly.

Regarding SY 1381, the CAO noted that USD 123,940,610 were presented as expenditure and USD 112,674,849 (over 90%) were found eligible. USD 7,158,936 were ineligible, USD 393,547 represented un-presented checks while the remaining USD 3,713,278 represented un-reconciled balances. The main concerns raised were that the ARTF/GOA financial management system needs strengthening:

- Bank reconciliation needs strengthening;
- The national authorities should have the responsibility for preparation of financial statements (in SY 1381 much of this had been done by the MA);
- A similar observation was done regarding the responsibility for preparing statements of expenditure (again the MA had been important for doing this);
- Modified cash basis of accounting (continuing to attribute expenditure to a previous SY once the actual SY had ended) should be abolished and a cut off point established;
- Control on non-salary expenditure needs strengthening;
- Records management needs strengthening;
- Procedures for monitoring ineligible expenditure need strengthening
- Lack of local staff capacity in MOF and ministries;
- External assistance often has the form of fire fighting rather than ensuring continuity and capacity building.

The CAO found, however, that the introduction of the computerized check clearing system had improved the situation considerably, and therefore expected better performance in SY 1382. Despite short-comings in the software package, the CAO recommended that it be kept, as it was reasonably simple and robust⁶.

Despite the deficiencies noted above, the CAO final verdict was that the ARTF is a well functioning arrangement, and that the MA was performing well against its terms of reference.

⁶ There have been suggestions to introduce more sophisticated public accounts software, such as Oracle or SAP. The experience with these more comprehensive packages is very negative, however: they tend to be costly to install and train, the annual running costs and licence fees are high, and they are much too sophisticated for the needs of a country like Afghanistan. It is worth noting that the Scandinavian countries consider Oracle and SAP as too costly and complicated for their needs, and instead use off-the-shelf software that has been modified to public sector requirements.

The Ministry of Finance has responded to the management letter and audit report from the CAO, and noted the measures it intended to take to address the issues raised.

The external accountability cycle is thus being put in place. Once the new Parliament has been elected, the expectations are that a Public Accounts Committee or similar will take on the policy review function, both discussing the budget proposals prepared by government, and debating the external audit carried out on the actual expenditures.

4.4 Assessment of ARTF's Recurrent Window Performance

4.4.1 Efficiency and Effectiveness

The World Bank, as the Administrator of the ARTF, has assumed the costs of running the Trust Fund. As compensation for this, it takes an overhead charge, which so far have been under one percent of funds provided by donors⁷. This is very low compared with what is standard for project execution contracts, where overheads typically can range from 5% up to over 10%. The ARTF, however, has a much larger funding base from which the overhead is being charged - so far about USD 900 million in paid-in contributions. But the costs of managing the ARTF are also lower than with project implementation since project management activities are handled by external contractors that are paid directly from the project budget.

The Bank has used this overhead to fund the Management Team and some other management costs including parts of the Financial Team, though the latter focuses mainly on IDA credits. These teams have been critical to the considerable improvements in disbursement and performance of the ARTF over last 12 months.

Both the "in-house" Bank teams and the MA have provided value-added not only to the ARTF funded activities, but are credited with "spill-over" quality improvements in the overall PFM. Much of the credit for PFM improvements should of course go to the Afghani staff in the MOF as well as the various TA groups that are providing assistance to the different departments and units. But on the margin, the ARTF teams are seen to have provided valuable quality assurance and standards-setting services which have enhanced not only reporting back to the donors, but even more actual performance by public officials.

As PFM performance and hence efficiency has improved markedly over the last two fiscal years ("doing the things right"), GOA is also being provided with the resources to improve their overall budgeting and getting resources out to where actual services are to be delivered. This is being done in line with better articulated strategies (the SAF is so far the clearest example), so that ARTF contributions are targeted and utilized better (salary payments reaching the teachers on time, etc). The ARTF is thus contributing to GOA also "doing the right things" - improving effectiveness.

Some GOA officials have argued that the alternative to the ARTF could be direct budget support, and that this might have been more efficient. There is, however, little support among the donors to provide direct budget support at the present time, which is also acknowledged by the most GOA officials.

⁷ From the Administrator's financial report it can be seen that the Bank has taken about USD 6 million as its management fee during the first three years of ARTF operations. In addition comes the interest income earned by ARTF balances, which particularly to begin with were significant. But it would be reasonable to also consider the fee of the MA as part of Bank overhead. This constitutes an additional USD 5 million. Together these costs come to a little over one percent of ARTF funds.

The most likely alternative to the ARTF would have been donor-by-donor funding, largely through specific projects. This would have been much more costly, not least of all to the government. Given the attitudes of some of the donors, it is also likely that GOA would have had major problems mobilizing the requisite resources for O&M expenditures over time. This would have involved negotiations, endless rounds of target setting and reporting, etc. The lessons from African countries that have had to deal with a fragmented and non-harmonized donor community are not encouraging.

Overall, the ARTF Recurrent Window must therefore be seen as a major success in terms of efficiency and effectiveness. It was established in very short time, it put in place performance standards (that have been adjusted over time) so that the continued funding has been paralleled with improvements in GOA's ability to allocate, fund and track performance. The funding has been on-budget and has thus contributed to strengthening transparency and capacity building by using and developing GOA's PFM systems and tools. Finally, the MA has provided real value-added and has therefore been a cost-effective addition to the overall Recurrent Window management.

4.4.2 Relevance and Impact

All stakeholders, whether GOA or donor, agreed that the Recurrent Window has been an indispensable contribution during the difficult period of re-establishing the nation-state and putting in place a viable public sector that can provide essential services to the population. Given the funding gap that necessarily will continue to exist for some time to come, the Recurrent Window will continue to play a strategic function.

The Impact is largely seen in two areas. The first is in the field of PFM itself. This is partly due to the specific work that the MA is carrying out, pushing for enhanced performance and demanding compliance with fiduciary standards. The other is that since the ARTF is channeling resources on-budget, an increasing share of total funding is being handled by the national PFM systems, improving transparency but also overall accountability for resource usage. The weakness is that many of the advances remain dependent on external TA for continued performance, so that longer-term impact remains conditional on GOA being able to develop its own capacity and governance systems.

But Afghanistan has in fact performed well beyond what could reasonably have been expected only two years ago in terms of overall PFM, thereby substantially strengthening the government's arguments for more donor support being channeled through the budget system. The ARTF has shown the way and acted as a pilot and assumed the learning costs and risks. The Impact here may therefore be further untying of donor funding and a more rapid transition to general budget support.

The other area of Impact, is through better service delivery due to resource availability. While paying teachers' and nurses' salaries contributes to direct output delivery, the longer-term Impact will be seen in the institutionalization of better social services, and this in turn should over time be captured by enhanced literacy and health status indicators. Overall, the Recurrent Window is funding the basic public services that any society depends on for its longer-term growth and development.

At a more subtle but perhaps more important level, the continued ARTF funding is ensuring that the legitimacy and credibility of the state is strengthened, providing a more solid basis for political stability, national security, and a more open and enabling environment for business and civic activities. While these are more fragile gains, and

the longer-term impact can conceivably be reversed, the systems for delivering and the levels of the funding are contributing to making the longer-term impact possible.

One concern that has been raised is that continued ARTF Recurrent funding may undermine own efforts at revenue mobilization - that the ARTF becomes a substitute rather than a complement to own efforts. This would weaken rather than strengthen the longer-term impact of the funding.

It is this mission's firm conviction that this concern is misplaced. GOA officials and the official documents clearly have revenue mobilization and financial independence as primary concerns, and the ARTF is thus providing the bridging funds necessary before the national economy is able to generate the required own-funding.

4.4.3 Institutional Arrangements and Flexibility

The institutional arrangements discussed in chapter 3 have been found to be good. The roles and responsibilities are transparent, the set-up is flexible and largely un-bureaucratic, though in the early phases GOA officials felt that both the MA and the Bank were too rigid in applying reimbursement criteria.

There were also problems with disbursement and reporting in the early phase, prompting the Bank to establish the ARTF teams that have led to considerable performance improvements.

Information dissemination is seen as good and transparent due to the early and comprehensive use of the Internet. This has been, in the context of Afghanistan, an innovative step that has set a standard for other activities in the country.

4.4.4 Finances and Sustainability

The sustainability of the early achievements is of course highly uncertain. Afghanistan is still facing a number of destabilizing factors that include the power and local political hegemony of some warlords; the opium production economy; a revenue base that remains sensitive to customs income rather than taxes from in-country productive activities; and continued political challenges from the Taliban and perhaps other regionally-based movements.

The *trend*, however, appears to be towards greater stability. If this can be maintained, what has so far been produced in terms of better PFM systems and derived welfare enhancements should be sustainable. The government has shown that the areas to which ARTF funding is flowing remain priority, so the political will for continued efforts in these fields seem assured also under the recently elected government.

Some donors have raised questions about how long their head offices will be willing to fund Afghanistan's budget⁸, and this may be the bigger financing and sustainability challenge. This issue will be addressed in the last chapter, since this links in with the future of the ARTF in general. Here the problems of internal revenue mobilization and fiscal restraint are raised, since clearly the donors' commitment will be related to what is seen as the authorities' own contributions to a fiscally sound public sector.

⁸ One donor made the comment that "we would like to be more heavily involved in the social sectors instead". When the rather obvious was pointed out – that the recurrent budget *is* largely for social sector services at the primary delivery level and thus directly poverty reduction relevant – there was a pained silence. The lesson from this is that the ARTF will need to continue hammering home what the funding in fact is being used for.

4.4.5 Capacity Development

The ARTF has several important CD aspects. One is that the MA has changed its operational approach and is contributing to strengthened procedures and quality standards. Furthermore, by tracking the actual flow of funds to the end-users or beneficiaries, the MA has identified deficiencies in the system and come up with proposals for corrective action, which is capacity building. Providing the funds on-budget is systems enhancing and confidence building, and this is seen by the fact that flow of decisions and financial resources through the system - down to district and sector levels - is improving.

What is lacking is an explicit strategy for maximizing CD impact. The changes to MA procedures was not planned but simply evolved through dialogue amongst the parties. The ARTF teams in the Bank office have continuous discussions with their counterparts in the MOF, but focusing on operational issues, not on CD. The ARTF is funding a number of TA activities through the Investment Window (see next chapter), but this is not linked with either fiduciary concerns or CD issues on the recurrent side. The CD effects are therefore positive but *ad hoc*.

4.5 Conclusions and Recommendations

The main *Findings* and *Conclusions* are the following:

- Afghanistan has put in place most elements of a comprehensive public finance management (PFM) system, and is now working to both increase own revenue and maintain fiscal restraint.
- The MA has supported the development of the PFM by demanding compliance with fiduciary standards, adjusting these standards to the realities of the country, and training public officials in implementing them. During the first phase, the MA focused on enforcement of general standards and was criticized for being too rigid in applying them. Subsequent work focused on verifying the payroll – where problems so far identified are seen as relatively minor – and lately has focused on O&M. While ineligibility was on average around 80% last fiscal year, it fell to just over 2% during the third quarter of SY 1383 (October-December 2004).
- This rapid improvement is partly due to MA and MOF training and performance monitoring, but even more to MOF handling advances correctly and reducing ministry allotments equivalent to ineligible expenditures submitted in the previous period.
- Both Efficiency and Effectiveness of the Recurrent Window are seen as very good, not least of all because funding is provided on-budget and thus contributing to improved PFM, transparency and accountability.
- The Relevance is seen as high and will remain so as the funding gap over the coming period will remain high. Impact is seen primarily in PFM improvements, but also in terms of public service delivery in key areas like health, education, basic infrastructure. Achievements are fragile, however, dependent on external TA and continued improvement in national stability and security.
- The institutional arrangements are transparent and flexible, reporting is good and accessible through innovative use of the Internet. But continued donor funding for the recurrent budget is dependent on GOA being successful in mobilizing own

resources and showing a strong political commitment to achieving financial sustainability over a reasonable time horizon.

- The operations of the Recurrent Window and of the MA are providing some capacity development, but this is largely *ad hoc* and not based on a longer-term CD strategy.

Based on the above, the Evaluation Team's ***Recommendations*** are as follows:

- The structure and priority of the Recurrent Window should be maintained. The World Bank in close collaboration with the national authorities should continue to encourage the donors to provide untied funding for the budget through the ARTF as the most efficient and effective support modality.
- The use of a MA has proven to be highly valuable and should be continued.
- A CD strategy should be developed as part of the budget support (Recurrent Window), to ensure that Afghanistan's PFM derives maximum benefits from this.

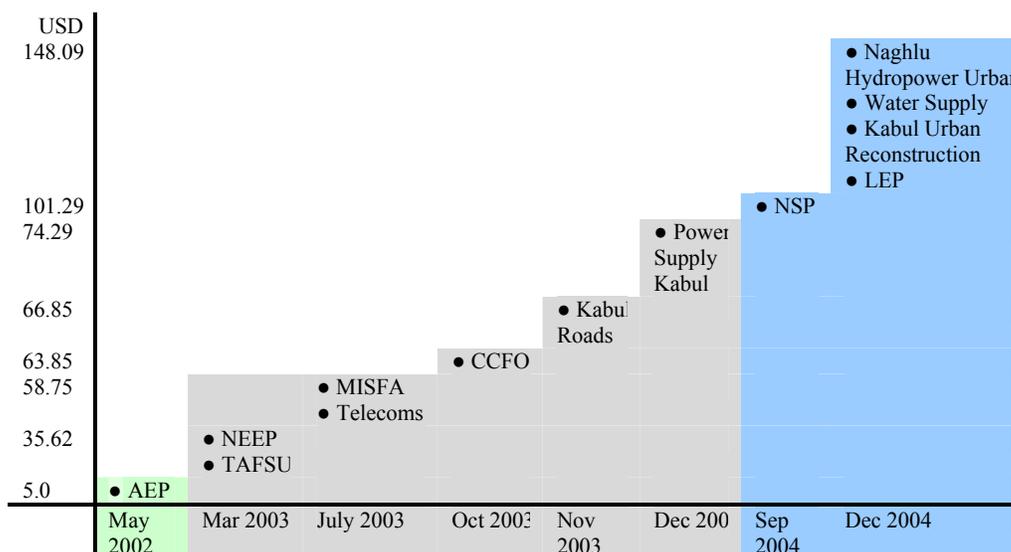
5 The ARTF Investment Window

The ARTF can either finance free-standing projects or co-finance IDA or other donor funded projects. Only 3% of the total commitments were approved in 2002, 47% in 2003 and 50% in 2004. As a result of increasing contributions by donors to the Investment Window and the approval of projects co-financing IDA grants, project approval rate has substantially increased at the end of 2004.

By the end of 2004, there were nine active projects: (i) Afghan Expatriate Program (AEP) which now has an added project, the Lateral Entry Program (LEP); (ii) Technical Assistance & Feasibility Studies Facility (TAFSU), (iii) National Emergency Employment Program (NEEP), (iv) Microfinance Project (MISFA), (v) Telecommunications, (vi) Kabul Roads and Drainage Project (Kabul Roads), (vii) Power Supply to Kabul, (viii) Financial Management Capacity Project (CCFO), and (ix) National Solidarity Program (NSP).

In December 2004, four new projects were approved: (i) Naghlu Hydropower station; (ii) Urban Water Supply; (iii) Kabul Urban Reconstruction; and (iv) the LEP. This brought total project commitments from USD 101 million to USD 148 million. In February 2005, support to the Interim Poverty Reduction Strategy Process (I-PRSP) was accepted, and the Education Quality Improvement Project (EQUIP) has in principle also been approved.

Table 5.1: Project approval and commitments to December 2004.



5.1 Projects in the Investment Window

This section provides only brief project overviews with an account of progress, since more complete project descriptions have been presented in the reports to donors and are available on the ARTF web site, www.worldbank.org.af.

5.1.1 Afghan Expatriate Project (AEP) and Lateral Entry Program (LEP)

AEP Project is to attract 60 highly qualified expatriate Afghans into the public administration for a short period of time – normally six to twelve months – to provide high-level policy and institutional advice and capacities to the public sector.

While the AEP was the first project approved, in May 2002, actual implementation only started up in July 2004. Then the Independent Administration Reform and Civil Service Commission (IARCSC) contracted the International Organization for Migration (IOM) as project implementer. As of February 2005, 21 expatriate have been placed in line ministries.

LEP Project is to (i) provide short to medium term capacity to ministries primarily in agencies where the Priority Reform and Reconstruction (PRR) effort has been slow to take off⁹; (2) lay the foundation for the reform process in ministries and government agencies that are currently not under the PRR process; and (3) train, mentor and motivate regular post holders to work more efficiently and more effectively for the government.

The LEP seeks to recruit 1,500 qualified Afghan professionals to act in senior civil service positions with a pay of up to USD 2,000/month on contracts for two years, renewable once for one additional year. LEP was approved in December 2004 and the project will be implemented by the IARCSC.

5.1.2 Technical Assistance and Feasibility Studies Unit (TAFSU)

TAFSU is to assist GOA with technical and professional skills. The project provides TA to line ministries to design programs and projects suitable for funding by key development partners or private sources. The specialists recruited help guide the preparation and supervision of reconstruction and development activities, and to design and supervise feasibility studies. In addition, the project funds feasibility studies for investment projects.

Of the USD 14 million approved, less than USD 5 million was disbursed by mid-January 2005. However, according to the Afghan Reconstruction Development Services (ARDS) which manages the project, by September 2004 there were commitments of USD 12 million and a further USD 1.7 million was earmarked by February 2005. A further application to ARTF is in process.

The project responds to a need to bolster line ministry capacities in the development of projects. It was one of the first under the Investment Window, but its initial performance was poor. The company contracted for recruitment of individual consultants managed to disburse funds rapidly but there was no clear accounting for what the international TA was doing. Consultants were hired on generous terms with poor terms of reference and no counterparts. The consultants were changed in July 2004, with a really remarkable improvement in results. The new management firm developed a new implementation strategy, enabling them to recruit 21 consultants during the six months of their contract period. They insisted on interviews by the line ministry concerned, they paid consultants based on submission of monthly progress

⁹ The PRR is an important step in the authorities' efforts to rationalize and modernize public administration. It is to identify key tasks in a ministry, define the critical skills needed to produce them, and through enhanced salary remuneration against specified performance criteria ensure that the right persons are recruited to those posts.

reports, and they conducted exit interviews with departing staff. Table 5.2 below outlines their recruitment process. They also rationalized consultants' costs including review of travel, housing and salaries, resulting in a saving of USD 1.3 million.

With the completion of that contract, the management of TAFSU is now with the ARDS, which has produced a TAFSU project implementation manual – a detailed (119 pages) statement of TAFSU purpose and methods. This is the only ARTF project where there is no international management, so ARTF Manager acts as task manager.

Through the second TAFSU component, ARDS is involved in negotiating contracts for feasibility studies. This component is where disbursement has been the slowest with delays in finalizing TORs, evaluating bids, and getting contractors in place. The project is also seen to have provided unsatisfactory reporting to ARTF.

Table 5.2: TAFSU International TA recruitment

#	Process Steps	Who	Average duration
1	Receipt of a Letter of Request	Ministry	N/A
2	Drafting of Terms of Reference	Ministry	1 week
3	Clearance received on LoR and ToRs	World Bank	2 weeks
4	Advertising	TAFSU	3 weeks
5	Interview process first round	TAFSU	2 weeks*
6	Interview process second round	Ministry	2.5 weeks
7	Candidate final selection	TAFSU and Ministry	N/A
8	Clearance received on candidate selection	World Bank	0.75 weeks
9	Offer issued to candidate	TAFSU	N/A
10	Offer accepted by candidate	Candidate	1 week
11	Contract drafted	TAFSU	Not significant
12	No objection received	World Bank	1.5 weeks
13	Consultant on board	Consultant	3.5 weeks
	Total Average Duration		About 3.5 months

* Overlaps with advertising time allowance since candidates are interviewed on a continuous basis.

Source: Human Resources Activity Report, ARDS, September–October, 2004.

5.1.3 Financial Management Capacity Project (CCFO)

The objective is to improve the financial management capacity of strategic line ministries by providing international Counterpart Chief Financial Officers. The project has three components: (i) services to assist budget preparation processes including programming activities and preparing budget estimates of wage, non-wage and development expenditures; (ii) procurement and installation of computers for financial management systems designed to assist the development of systems and methods of standardization between line ministries; and (iii) services to develop and carry out training sessions on core financial management disciplines to key staff in selected line ministries.

Under the first contract, eight CCFOs were to have been hired, though on average only six have been in post. The project is not seen as very successful, in part because a number of the ministries do not have their CFOs in place (the legislation that will

formally establish and define the post has still not been passed), the coordination with other related TA projects has at times not been smooth, line ministries have been unclear on how to take best advantage of the international expertise, etc.

5.1.4 Telecommunications and Improvement of Power Supply to Kabul

The telecommunications project consists of three parts: rehabilitation of the satellite earth station in Kabul; a microwave project for expansion and improvement of transmission links; and the installation and operation of an efficient billing and collection system for the digital network for Kabul and neighboring areas. The power supply project also has three components: rehabilitation of the hydropower station; transmission and distribution materials, and street lighting in Kabul.

These two emergency infrastructure projects were GOA priorities, where the ARTF acted as "funder of last resort". Both projects are reconstruction projects that have an economic justification since they will contribute to enhanced revenue collection. In the power project the ARTF supplements support provided and managed by KfW. The telecommunications project ran into delays because the original finances turned out to be insufficient. The ministry expressed the familiar view that disbursements were painfully slow through the Special Disbursements Unit of the MoF. This is a relatively strong ministry and has ambitious investment plans, so delays on implementation and disbursement are an irritant. But there was also an understanding of the need to work through the budget. Apart from this issue, neither ministry had problems with the ARTF itself, and implementation is proceeding.

5.1.5 Kabul City Roads and Water Drainage Project

The project was to improve the transport services on roads within the city through the rehabilitation of high priority road sections. Approximately 45,000 tons of asphalt was used for pothole backfilling, and 155 km of asphalt road was repaired. It has also repaired water drainage systems along important thoroughfares.

ARTF funding supplemented resources provided by the German government through KfW, who was responsible for contracting the implementation partners. The project was addressing a clear emergency need since Kabul's roads had suffered prolonged neglect. The work as has been completed with a high degree of satisfaction with the results. The project provided direct employment (28,000 days by September 2004), along with a series of subcontracts issued to local companies for supplies.

The Kabul municipality was the host for this program and has been closely involved, including in the implementation of works until the contracts were signed, late in the project, with new private companies.

5.1.6 National Emergency Employment Program (NEEP)

NEEP is to provide employment in rural areas at a minimum wage, as a safety net, to as many people and in as short a time as feasible. NEEP-1 is also designed to repair infrastructure and improve key rural access roads through short-term emergency employment opportunities on labor-based rural roads sub-projects.

NEEP is managed through a Joint Program Management Unit (JPMU) that covers the three ministries involved: Ministries of Public Works (MPW), Rural Rehabilitation and Development (MRRD) and Irrigation, Water Resources and Environment (MIWRE). It is to (i) develop a national database of contractors; (ii) standardize tender documentation; (iii) establish accountable and transparent bid evaluation

procedures; and (iv) train in international supervision procedures. NEEP is co-financed by IDA and a number of bi- and multi-lateral donors.

NEEP has been implemented through the following arrangements:

- MRRD contracted CARE International as Oversight Consultant to manage implementation of sub-projects (of which about 70% are for road repairs and the balance for repair of schools, irrigation, and drinking water supplies) by local and international NGOs in 12 provinces. Implementation began in October 2002 and was completed by March 2004.
- The Ministry of Public Works contracted UNOPS to help oversee contracts for road repairs using local private contractors and local *shuras* through community contracting procedures in 31 provinces. Implementation started in January 2003 and was completed by October 2004.

To date, about 3 million days of employment has been created; 4,100 km of roads have been repaired; 46 sub-projects for rehabilitation of irrigation systems, schools and water storage have been completed. A total of 316 sub-projects were completed.

5.1.7 National Solidarity Program (NSP)

NSP is to strengthen community level governance, and to assist in reconstruction and development of rural communities. The project funds block grants for reconstruction and development activities through a facilitated participatory planning process. It provides community facilitation and project preparation as well as strengthening of communities' capacity in financial management, procurement. Technical skills and implementation support is provided to the Ministry of Rural Rehabilitation and Development (MRRD), and the project funds external monitoring and evaluation.

The NSP is implemented by MRRD. Program management is supported by an internationally recruited Oversight Consultant with a total of 20 international and 400 local staff. 21 facilitating partners (FPs) comprising Afghan and international NGOs plus UN-Habitat implement the program at the community level, with a combined field staff of around 3,200. The NSP thus represents a massive "push" by GOA to reach out to the communities.

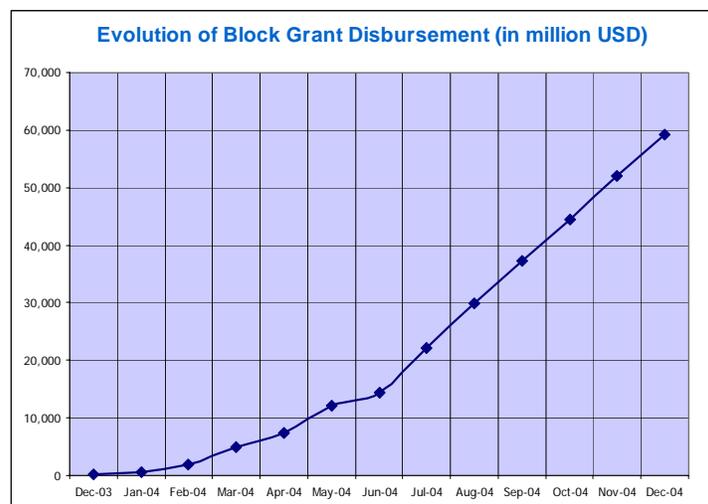
In response to GOA request, NSP coverage was expanded from the original 800 villages at appraisal, to 4,500 villages in the first year. By September 2003, the FPs were contracted and in place, supporting community mobilization, election of Community Development Councils (CDCs), subprojects preparation and CDC capacity building.

By the end of December 2004, USD 101 million were committed to 5,445 projects, and over USD 59 million had been disbursed. Over 4,200 CDCs in 32 provinces had received block grants of an average of USD 30,000 based on average community size of 150 families.

In May 2004, an independent review of NSP was carried out, assessing performance by all 21 FPs in 25 provinces, interviewing around 2,500 informants (see Altai Consulting 2004). The study provided assessments of each of the 21 FPs, and rated their performance along a series of common indicators. The study comes across as very informative, ranking the FPs by performance and then classifying them along key dimensions, thus providing management with a clear understanding of where the good performers and the problem areas are. However, overall the conclusions are

highly positive, with NSP progressing well in nearly all of the provinces visited and with a strong and supportive interest in the program around the country.

Table 5.3: NSP Block Grant disbursement over time.



Source: Oversight Consultant's Quarterly Report, 1st October – 31st December, 2004.

Based on the evaluation and due to a policy review by the new government, NSP implementation in 2004-2005 will change. The rate of program expansion will slow to allow the FPs to catch up on the backlog of community activities.

The first year of NSP was costly: it cost a dollar to deliver a dollar. This was due to the long and costly mobilization phase. The goal is over time that delivery costs will be 25 cents to each dollar delivered (20/80 share of resources).

5.1.8 Microfinance Investment Support Facility (MISFA)

MISFA was established in 2003 to meet the demand for microfinance. In building a financial system that would serve the country's poor, MISFA's approach was to "get it right" from the start by having all donor support channeled through a competent technical agency. As a funding vehicle, MISFA therefore not only ensures donor coordination, but also enables donors to outsource "due diligence" work and monitoring of investments to experts in the field. It also streamlines reporting and fundraising procedures for microfinance institutions, allowing them to concentrate on quickly building up retail capacity.

With initial funding of USD 1 million, MISFA was established in the summer of 2003. It functions as a microfinance apex organization supporting all major microfinance institutions (MFIs) operating in Afghanistan. It provides grant funds for capacity building and loan funds for disbursement to clients. MISFA closely monitors performance of the MFIs and second and subsequent tranche releases are dependent on strict performance criteria relating to the use of funds and the size and quality of the loan portfolio.

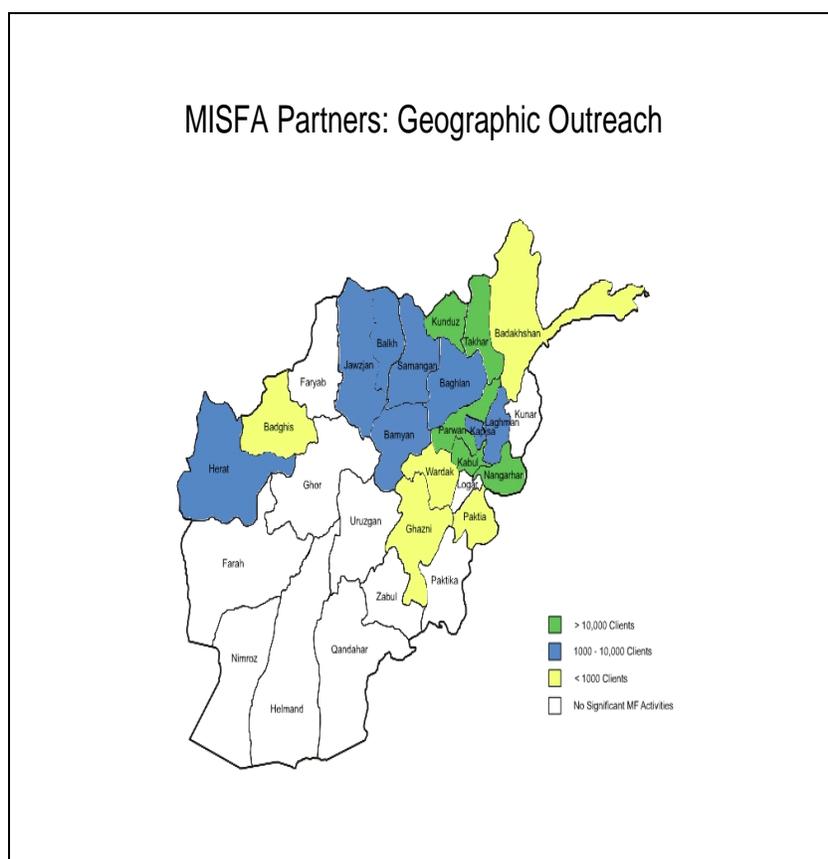
MISFA has been able to garner donor support and rapidly increase its activities (Table 5.4). It has yet to complete its 18 month pilot phase, but its budget from March 2005 is already nearly USD 50 million.

Table 5.4: The Projected Growth of MISFA – 2003-2008

	June 03 – March 05	April 05 – March 06	April 06 – March 07	April 07 – March 08
Total USD	25 million	48.5 million	57.4 million	57 million
MISFA	13.2%	6.0%	3.5%	3.1%
Sector TA	5.6%	2.0%	1.8%	1.3%
MFI Grant	49.2%	39.0%	34.4%	27.0%
MFI Loan Fund	32.0%	53.0%	60.3%	68.6%

A core challenge for MISFA has been the justification of very high capacity building expenditure and a lower proportion of outlay on funds for actual disbursement as loans. The MISFA argument has been that the high percentages on grant support to MFIs are front-end or start-up costs, and that loan funds will take over as the dominant use of donor funds. This is exactly what the table shows. As the map below documents, MISFA partners are already operating in over half the provinces.

Figure 5.1: Overview of geographic reach of MISFA, end 2004.



The key reason MISFA has managed to grow quickly is its variety of partnership arrangements covering different service delivery models. Table 5.5 shows the outreach as at October 2004. Starting from a near zero base in 2003 to nearly 60,000 borrowers is very impressive. For impact assessment these numbers should be

supported by data on changes to the poverty status of borrowers. At this stage it is only possible to infer from loan utilization records, and the odd case study, that positive changes have occurred.

Table 5.5: MISFA Client Activity: October 2004

	Active Loan Clients	Loan Portfolio Outstanding (\$)	No. Savings Clients	Savings Outstanding (\$)
BRAC	46,809	3,034,290	65,777	662,542
AKDN	3,334	1,948,229	0	0
FINCA	3,260	363,684	3,499	31,443
Mercy Corps	1,587	139,815	0	0
CARE	304	90,349	1,832	55,807
WfW	576	81,739	0	0
CHF	304	98,200	0	0
WOCCU	0	0	892	4,651
DACAAR	1,272	89,516	6,480	14,137
MADERA	210	23,136	0	0
Parwaz	560	40,000	560	5,429
Totals	58,216	5,908,958	79,040	774,009

Source: MISFA presentation to World Bank supervision mission, December 2004.

MISFA is expected to grow as the sector grows and training and oversight functions expand. The funding in the short-term will be primarily through the ARTF. It is expected that MISFA, as an authority to establish and monitor fiduciary standards of service providers, will be a conduit for other funds, including commercial funding, for sector expansion. This change may be beneficial since the ARTF has, in a sense, provided an additional layer of control that duplicates MISFA functions. As administrators of the ARTF, the World Bank has applied IDA rules, both direct MISFA funding and that of its partner MFIs; yet, MISFA is set up expressly to monitor the performance of these MFIs by developing their capacity and supporting their growth through grants and loans which it itself monitors.

5.2 Structure of Portfolio

The ARTF projects can be grouped into three broad categories: infrastructure, community development/service delivery, and capacity development (CD) in the public sector. As shown in table 5.6, committed funds are highest in the infrastructure and in the community development project groups. Until December 2004, however, nearly 60% of the funds were committed to the community development group.

With the exception of the telecommunications project, the infrastructure projects have all been financed jointly with or as a follow up to projects financed by KfW or IDA. Until the latest bunch of projects approved in December 2004, they have essentially been emergency reconstruction activities.

The community development/service delivery projects are co-financed by a large array of donors. This group of programs aims at nation building through direct engagement of and interaction between civil society organizations, communities, private sector actors and levels of government. They target all provinces and also support community development plans. In addition, they generate emergency (NEEP) and non-emergency (Microfinance) employment for poor men and women. Together, they have been delivering small-scale infrastructures to communities (water wells,

irrigation channels, secondary roads and bridges, etc.) and building up the private sector by contracting local small-scale businesses.

The capacity development projects have focused on capacity in the public sector. AEP and LEP are recruiting Afghani expertise that is currently not in the public sector, to strengthen management throughout the public sector – AEP at the top advisory level, LEP at senior technical levels. TAFSU and CCFO are instead bringing in external TA, CCFO in the field of PFM to the line ministries outside the MOF, while TAFSU is helping line ministries more in their technical fields.

Table 5.6: Grouping of ARTF projects and total investment by group.

<i>Infrastructure</i>	<i>Community development/ service delivery</i>	<i>Capacity Development</i>
Telecommunication	NEEP	AEP
Kabul Roads	MISFA	TAFSU
Power Supply to Kabul	NSP	CCFO
Naghlu Hydropower ¹		LEP ¹
Urban Water Supply ¹		
Kabul Urban Reconstr ¹		
<i>USD 60.4 million ²</i>	<i>USD 60.6 million</i>	<i>USD 27.1 million</i>

(1): Projects approved in December 2004.

(2): USD 16.6 million before December 2004.

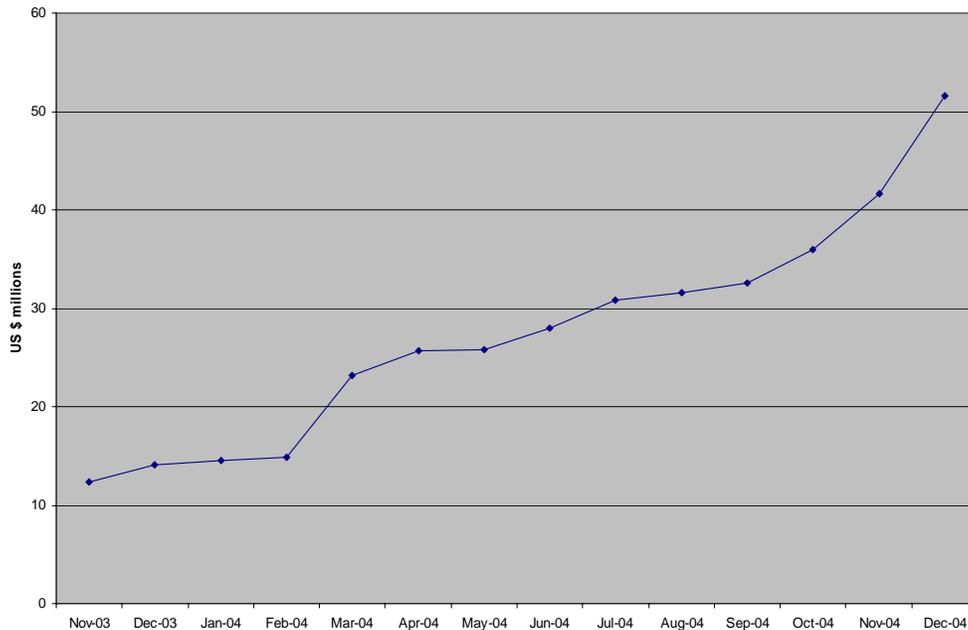
There is a discussion regarding whether the ARTF ought to have criteria that prioritizes the three categories. The current consensus seems to be the following:

- Infrastructure projects should not be funded over the ARTF. The newer infrastructure projects are typically capital intensive ones for which concessional loans are readily available, and for which burden-sharing mechanisms for the future O&M costs can be mobilized, or services can even be charged for directly (water and energy).
- Grants funds should focus on public goods and poverty reduction activities. The community development projects are highly relevant for the poverty reduction concern, and some of the funded activities also have public goods aspects (public water, social sector infrastructure for primary service delivery etc.). Capacity building in fields like PFM and public sector management are typical public goods. How to choose between these two categories is therefore a question that will be returned to in the last chapter.

5.2.1 Disbursement over Time

Disbursements (Figure 5.2) have grown rapidly recently after a slow start. The reasons for the slow rate of disbursement up until the end of 2004 were largely the weak capacity in GOA to prepare project documentation and implement activities. There were also disbursement delays due to Da Afghanistan Bank's (DAB) poor capacity to execute transactions promptly and provide other banking services (ARTF project special accounts are opened and maintained by DAB).

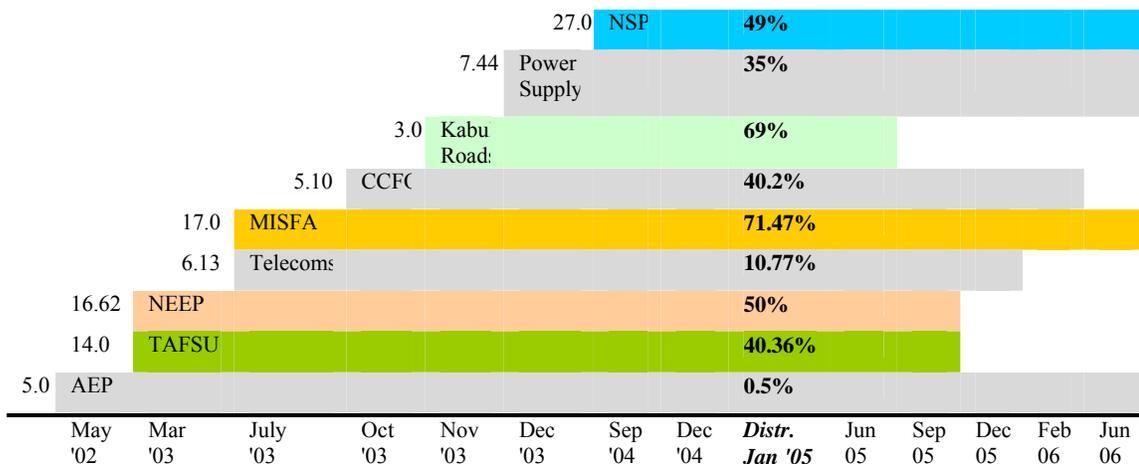
Figure 5.1: ARTF Investment Portfolio - Cumulative Disbursements



Source: Administrator’s Report on Financial Status, September 2003 to January 2005.

But some of the projects were designed to first build capacity and only later increase disbursement, such as with NSP and MISFA. Community development projects in particular require contracting and coordination of numerous implementing partners and a lengthier period for community mobilization and planning. Table 5.7 shows disbursements by projects, where AEP is the key "laggard".

Table 5.7: Project disbursement as a % of total commitment.



The World Bank, as noted in the previous chapter, strengthened the ARTF management team and brought in staff to facilitate financial management. Lack of familiarity with IDA procedures (used for ARTF projects) was a major source of delay. The Kabul-based management team runs regular clinics, also involving DAB

and MOF staff, to assist implementing partners with procurement and disbursement rules and required paperwork.

5.3 Governance of the Investment Window

All proposals for activities that are to receive ARTF funding come from the MOF. These can in principle come from any line ministry in the Government, but must be accompanied by a justification in terms of importance to the National Development Framework (NDF) and the National Priority Programs (NPP) (see Annex F).

The MC is responsible for ensuring projects comply with selection criteria and are adequately prepared. Most ARTF stakeholders consulted expressed satisfaction with the approval process although concerns were expressed regarding the lengthy period for project approval. However, it was recognized that many delays in pre-approval procedures occurred in the MOF, and there were no arguments offered for changes in current pre-approval procedures such as diagnostic and feasibility studies. Proposals for activities that co-finance IDA projects have had more rapid approval since all pre-approval information (diagnosis, costing, implementation method and management, etc) has been produced by the World Bank.

5.3.1 Performance Management

The ARTF management team has the responsibility to monitor and report on the progress of projects. For those projects co-funded with IDA, the Bank has a task manager who tracks developments. Performance management is therefore usually a cooperation between ARTF management, Bank task managers, and GOA staff or external implementing partner responsible for managing projects.

As stipulated in project agreements, project management is to produce quarterly reports available to ARTF management. Reporting, however, has started late and has not been consistent. While some projects have eventually built capacity to report quarterly (NSP, MISFA, TAFSU under current management), others have not been reporting consistently (NEEP, TAFSU under the first contract). Monitoring and reporting on projects' performance has therefore been uneven.

Three reasons regarding poor reporting surfaced:

- Unclear line of responsibility between GOA (staff in line ministries responsible for managing ARTF projects) and its implementing partners.
- GOA's general lack of monitoring capacity.
- Early project agreements did not provide ARTF management with a legal basis to enforce reporting requirements from implementing agencies. TAFSU under the first contract did not provide a single report since it was not part of the contract.

Uneven reporting is a cause for concern because it restricts the ability of the ARTF team to verify financial flows against project outputs. No systematic approach to reporting has been undertaken by GOA yet, in large part because this is a function of the weak management capacity in most of the line ministries. IDA has provided a standardized reporting format to the MOF for use by line ministries in order to facilitate procedures and enable portfolio analysis. In addition the ARTF management team has been active in monitoring projects' progress by coordinating with Bank task managers (where they exist) and project management. Projects co-financed with IDA

thus have better reporting as they follow normal IDA procedures, with supervision missions and reporting.

But overall the Investment Window does not have clear, consistent and on-time performance reporting. This part of the ARTF hence has some ways to go to satisfy the Performance Management aspiration of the Paris Declaration. It also means that the ARTF has not contributed in any systematic way to improved project management and PFM as far as the development funding goes.

5.4 Portfolio Performance

5.4.1 Relevance

The investment window has funded projects that are within the National Priority Programs of the NDF. It has been disciplined in applying these criteria, which has led to at least one urgent request (rural water) being returned because it did not meet them. The Investment Window has been responsive to investments identified by GOA, and has also accommodated preferences of donors to specific projects. Upon request from the MOF, it has co-funded investments developed and managed by other agencies (IDA and KfW). In some cases these investments have occurred because the ARTF was a readily accessible source of funds (e.g. for the telecommunications project) and its use was used to speed up disbursement and service delivery.

One key relevance of the ARTF investment window is that it has supported the strengthening of government ownership since MOF and the budget process has final say regarding project selection. But this has still largely been a *supply-led* agenda since donors have been closely involved in identifying the activities in the priority programs, and then supported them through the ARTF.

The CD group is composed of projects whose design represents "good practice" and innovative approaches to public sector capacity building. The LEP can make a strong contribution in making GOA's PRR feasible while TAFSU provides short and medium term institutional support for policy implementation. Both of these projects have sustainability of capacity and GOA ownership as a central concern.

Projects in the community development group are making a strong contribution to GOA's policy of integrating rural communities in Afghanistan's development, both at the decision making and implementation levels. All the three projects in this group have been delivering rural infrastructures based on community's prioritization and utilizing rural labor, and thus providing employment.

5.4.2 Effectiveness

The infrastructure and community development projects have been more effective in achieving their objectives than the CD projects. Comparing objectives with outputs to date, projects such as NSP and MISFA have been highly effective. NEEP has been an effective program for generating employment rather than a safety net instrument. It is still too early for most of the infrastructure projects to assess their effectiveness. Only one (Kabul roads) has been completed; it has delivered according to its objectives.

The three community development projects are meeting their objectives. In the case of MISFA, the progress has been quite spectacular given the context. NSP is also now delivering services at community-level at impressive levels of disbursement. Across the investment window portfolio these are the two projects that have attracted most interest because they are the largest disbursing and have strong support from both the

GOA and the donor community. They are significant flagship service-delivery projects for the GOA (and ARTF) and are expected to enjoy continued support.

The CD projects have not, with the notable exception of TAFSU, performed so far. TAFSU is becoming an increasingly critical resource for both feasibility studies and expert but coordinated support to line ministries. A forthcoming TAFSU supervision mission will focus on the management and financing of TAFSU to ensure that it can respond to this challenge. But both GOA and ARTF management have expressed dissatisfaction with outputs and outcomes so far of the CCFO project.

Delays in the AEP were partly political and partly procedural, and the LEP has been through a long process of development and has only recently been approved. The evolution of a coherent civil service reform and restructuring process has inevitably taken time and there have been concerted efforts to ensure that these ARTF-supported inputs are consistent with that overall strategy. The PRR is now in place and disbursements under these two components should now speed up.

5.4.3 Efficiency

From an efficiency viewpoint – outputs achieved for inputs provided – most projects have high overhead costs due to the use of external managers/contractors for implementation. Within MISFA, the share of expenditures that has gone to CD, has varied from 40% to nearly 90%, with the balance being available for direct disbursements as loan funds. The variation reflects differences in operating and start-up conditions across MISFA partners. Concerned about the criticism, MISFA managers compared the costs to other country contexts and concluded that, given local conditions, CD costs were not excessive. However, for all investments, this remains a sensitive area and ARTF management is aware of this.

In addition, some projects have many intermediaries (NSP, MISFA), thus increasing delivery costs. Lack of effective competition in procurement has also negatively impacted the efficiency of projects. There are cases where the number of bidders was extremely small and bid prices are much higher than the costing estimates, even though they included a safety/security premium (telecommunication project). Projects have thus encountered cost-overruns and required additional funding and/or scaling back of scope of activities.

These facts, however, have not been confined to the ARTF Investment Window. The lack of domestic capacity, insecurity, and the need to rehabilitate and invest in basic infrastructure (buildings, vehicles, equipment) is the reality facing the country today.

On the other hand, ARTF gap-filling projects are integrated into IDA programs so as to increase the efficiency of the Bank's total intervention (Naghlu Hydropower and Urban Water Supply).

The possibility of contracting services more regionally (India, Pakistan, Iran particularly) may save costs especially on the very high international travel component in international TA and is being explored by GOA¹⁰. This trend could be pursued more systematically. In addition, GOA has phasing-out plans for some of its external management units such as NSP OC and through this means, as line ministries build capacity to manage projects, overhead as well as delivery costs can be reduced.

¹⁰ In the bidding for the procurement management contract for TAFSU, the costs of international travel were reportedly the most important difference between the successful and runner-up bids.

This underlines the importance of a recurrent theme in this report: the need for coherent institutional strengthening and capacity-building investments that will accelerate the phasing out of internationally-executed service delivery.

Finally, on efficiency, the ARTF is of course just one, relatively straightforward, trust fund operation and benefits from the global learning emerging from the many other trust funds managed by the WB. In interviews with the WB Washington trust fund management it was emphasized that IDA management is concerned to increase flexibility and reduce transaction costs whilst maintaining its fiduciary responsibilities. The aim is to reduce service costs and reduce disbursement delays.

5.4.4 Institutional Arrangements

There is a very diverse set of institutional arrangements within the ARTF. But weak national institutions and human resources has meant that GOA has been implementing most ARTF projects through contracting international consultants to manage projects' management units. This situation is not unusual in post-conflict situations when reconstruction and nation building are more urgent than building sustainable public sector capacity. In this sense, the implementation mode adopted by the ARTF Investment Window has been in line with national priorities.

External management units or project management units have been used in many countries when regular civil service staff were fully employed with existing responsibilities, or were unable to take on the additional tasks involved with major investment projects. The World Bank has a history of using what are known as Project Implementation Units (PIUs). The Operations and Evaluation Department of the World Bank made a review of the effectiveness of these units (World Bank 2000). With respect to post-conflict operations, a review of 157 Bank-supported operations in 18 countries concluded that the use of PIUs should be used only in exceptional circumstances or when there is no feasible alternative. However in such circumstances, there should be commitment to a monitorable phase-out plan.

As GOA begins to shift gears from a post-conflict to a development agenda, monitorable, phase-out plans for all of its current external management units should be elaborated. Phase-out plans should be in coordination with a CD plan (helping line ministries to build their management, procurement etc skills). While the lack of adequate numbers of counterpart staff in implementing agencies has been a generic issue, a coordinated CD/phase-out effort can draw from and actually make a more effective utilization of the CD projects in the portfolio.

MISFA stands out as an important innovation in institutional arrangements because it has established a wholly new organization which is now an autonomous public agency. This approach was driven by global knowledge of how apex organizations in microfinance need to be positioned in order to accommodate both public and private (commercial) investments. This is a little acknowledged but important example of how, even in difficult conflict affected contexts, it is possible to combine service delivery with a longer-term vision for service sustainability.

5.4.5 Capacity Development

Capacity development in the investment window has so far been designed and implemented at project level. In the case of the infrastructure projects, there has been little specific capacity building, reflecting the emergency nature of these investments. There are serious capacity constraints at mid-level in most of these institutions and

dependence on foreign expertise is likely to continue for some time even with more attention to domestic capacity building. Moreover, in the power sector the (ageing) human skills base is often rather specific – e.g. German-trained engineers for one power plant, Russian-trained for another with substantively different training outcomes and little scope for common understanding. Coordinating human resource development plans in these conditions is a long-term challenge.

The provision of TA in Afghanistan has been characterized by poor institutional arrangements, so the "best practice" approaches now being used by TAFSU are a very positive development under the ARTF. Similarly the AEP and LEP programs are being integrated into the PRR. Coordination is needed with other donors currently financing TA, in order to avoid gaps and reduce overlaps, and GOA needs to take the driver's seat. As SAF noted, "action is needed on the issue of the twin public sectors. That is, donors simultaneously fund their own and the international agencies' bureaucracies, while also underwriting the civil service bill for the government. This requires coordinated action including major investment in human capital and a commitment to invest in innovative schemes to level the playing field between the international agencies and the government as competing employers."

5.4.6 Impact and Sustainability

Five ARTF projects – Kabul roads, MISFA, NEEP, NSP, and TAFSU – have delivered substantive service to date. With the exception of TAFSU, these have all delivered services that directly reduce poverty. In the case of MISFA, case studies from BRAC, for example, have demonstrated that services have been used effectively to strengthen livelihoods. But for both NSP and MISFA more detailed study would be needed to fully evaluate their development impact. Such work is apparently planned.

The core principles of ARTF funding of investments – through the budget in response to national priorities – is designed to promote sustainable planning processes. The infrastructure group is, with the exception of the Kabul roads project which was addressing short-term needs, making investments that are clearly expected to be sustainable. They will generate revenues that should provide the resources for maintenance, and in the case of the telecommunications projects it is helping develop the mechanisms for collecting that revenue.

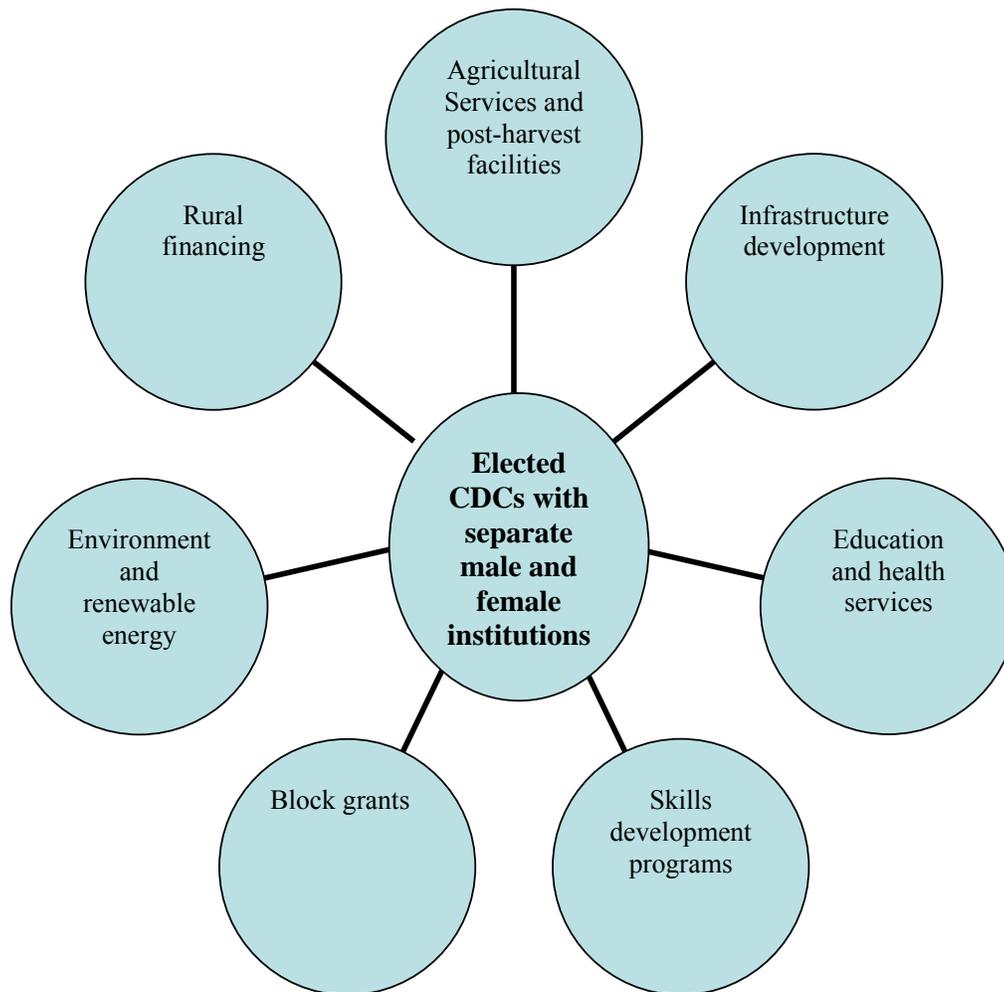
The human resource projects are in theory designed to support medium- to longer-term capacity. It is too early to say though whether the AEP and LEP investments will deliver on a sustainability agenda. TAFSU inputs are by their nature, short-term, but the sustainability of TAFSU itself is being served through the resources made available through the ARTF.

Perhaps the most critical sustainability issues relate to the community development and service delivery investments, especially the NSP and MISFA since the NEEP was, by design, an emergency operation. As noted above, MISFA has established itself as an autonomous institution and there is every reason to believe that it will provide a sustainable vehicle for microfinance service delivery. The threats to it are the possible promotion of microfinance through other channels that are less concerned with sector sustainability; the use of microfinance as a part of an alternative livelihoods strategy in the anti-poppy policy is one such threat since potentially large resources may be transferred to farms ostensibly as loans but with little institutional basis for effective operation of loans programs. MISFA management are keenly aware of this issue and are engaged in dialogue with other stakeholders to try and ensure

than any new microfinance initiatives are consistent with the principles which MISFA has established so successfully for the sector so far.

The most debated sustainability issue affecting the ARTF investment portfolio concerns the NSP and the CDCs. They have achieved a degree of legitimacy within communities, and slowly their legitimacy is being recognized as a governance resource. However, CDCs are still fragile and vulnerable structures and the role they will take in the future remains unclear. Thus far, the success of NSP is that it generated expectations on links between communities and the national government that were absent before. The MRRD has a vision in which the CDCs build on these links to make them the centre point for the delivery of rural services (figure 5.3). In this vision CDCs could prioritize and receive service needed from government and manage service delivery. They would also act as a community development forum utilizing locally raised resources. At this point, though, CDCs can only be seen as structures for testing the possibility of such a governance framework.

Figure 5.3: MRRD's Vision for the CDCs



Another key concern in the Impact area is that the ARTF has so far not expressed a clear gender policy, despite gender equity being a cross cutting issue in the Government's NDF.

Even so, gender equity was considered in some of the projects. CD projects have established indicators targeting gender equity. All three community development projects have gender mandates. NEEP has developed projects to accommodate the ability of men and women to work in road and other infrastructure projects. The establishment of female or male/female CDCs has been a requirement for the implementation of the NSP. Responding to the finding in the NSP evaluation regarding inequity between male and female CDCs in deciding priorities and managing block grants (Altai 2004), NSP has decided that at least 10% of the block grants must be decided and managed by female CDCs. MISFA is providing microfinance services for men and women and has established the *Women for Women* microfinance program.

But so far ARTF gender policy is *ad hoc* in that it greatly relies on the experience of the World Bank's task managers assigned to projects. At this point there is no gender mainstreaming guidelines applied to the Investment Window. As the Administrator of the ARTF, the Bank has been consulting with the Afghanistan's Ministry of Women's Affairs. The Ministry, whose leadership has changed after the election, is currently elaborating its own gender policy, including the mechanisms to articulate it across the Government.

5.5 Findings and Conclusions

The main *Findings* and *Conclusions* are the following:

- The ARTF project portfolio includes activities in three areas: infrastructure, public sector CD, and community development. Commitments stand at around USD 150 million with about one third has so far been disbursed.
- As far as prioritization among the three kinds of projects, most agree that grant funds should not be used for capital intensive infrastructure activities, since most can find concessional loan funding, can generate service income or other forms of burden-sharing funding. Grants monies should instead focus on public goods and poverty reduction activities: community development and public sector CD.
- Disbursements have grown slowly but recently increased rapidly, largely as early build-up of CD has led to greater absorption capacity by the projects (NSP, MISFA in particular).
- Performance and financial reporting started late and are not consistent. However, ARTF management has been active in monitoring projects in coordination both with World Bank task managers and project management (GOA and external).
- From an efficiency viewpoint, most projects have high overhead costs due to the use of external managers/contractors for implementation. Projects in the infrastructure and community development groups have been more effective than the CD projects.
- As GOA begins to move from a post-conflict to a development agenda, clear phase-out plans for all external management units should be elaborated. Phase-out plans should be in coordination with a capacity building plan.

- The ARTF has so far not developed a gender policy. While a number of projects have gender targets, overall this is *ad hoc* and dependent on individual task managers rather than systematic policy.
- CD in the Investment window has been designed and implemented at project level. The challenge is to raise the CD efforts to a programmatic or national level while assuring GOA's ownership and the sustainability of these investments.

6 Looking Ahead

The ARTF Recurrent Window has performed a critical function by providing the resources needed to run basic public services. It has furthermore done so in a way that is consistent with "best practice" approaches to trust funds in post-conflict situations. The question being asked is whether the ARTF is likely to perform as well under more normal circumstances expected in the years ahead.

Regarding the Investment Window, the activities so far funded have reflected the differing priorities of the GOA at the times funding became available. But there has not been a clear focus based on any strategic thinking regarding where ARTF funding could provide best value-for-money. The question is if this window therefore should be closed down, or if there are some obvious strategic funding areas where the ARTF would be particularly useful. These questions are addressed in turn below.

6.1 Recurrent Cost Challenges

In "Securing Afghanistan's Future" (SAF), GOA presents its vision of the future. This includes an analysis of how the budgetary situation is expected to develop over time. The intention is that by SY 1388 (four years from now), the government should be able to cover its wage costs, and four years later own revenue should be able to cover all recurrent expenditures. There are a number of caveats regarding these projections that need to be taken into account when looking at the continued need for recurrent budget funding by the donors.

6.1.1 Revenue Mobilization

The first concerns the revenue projections. As noted in chapter 4, revenues have increased almost two and a half times over the last two years, though from a very low base. By the time the wage bill is to be covered, according to SAF, revenues will have reached 8.5% of GDP, and four years later, when the full recurrent budget is to be covered, revenue will make up just under 12% of GDP. This, however, remains a low share of GDP.

But the revenue targets are expressed in AFAs, which means that the government not only has to reach the share-of-GDP rate, but also ensure that the quite high (non-poppy) GDP growth forecasts are attained.

The government thus faces two sets of problems: ensuring that the overall growth will take place and in sectors that will generate taxable income, and that it can collect the revenue foreseen. On the latter, it will face several challenges. The first is that a significant share of revenue collected is today not transmitted to the central fiscus. The State will need to be able to enforce its rule throughout the national territory in order to achieve this. The second is that a lot of taxes and other sources of revenue today on the books are not being collected, for a number of reasons: lack of tax data, insufficient collection and enforcement capacity, etc. The revenue collection system therefore needs to be strengthened. The third area is lack of up-to-date legislation that ensures a more equitable burden-sharing that addresses the legitimate tax concerns of the state versus creating the right incentives for national and foreign firms to invest in the country. The revenue paper that MOF is discussing is addressing these and other questions, and to some in the Ministry the revenue potential appears quite positive. The challenge is to implement all the tasks that are required.

6.1.2 Fiscal Restraint

While own revenue will remain a key task for MOF, fiscal restraint will also be a challenge. The first thing is the notion that the state can provide a satisfactory level of basic public services on a 12%-of-GDP revenue base¹¹. One possible contradiction here is that if the GDP-growth rates are lower than planned for, not only will the 12% of GDP in itself be an insufficient funding base, but the lack of economic growth may create a need for even *greater* public services. This is because in a situation where nation building and state legitimacy is still incipient, lack of direct impact on household welfare through economic growth may require other visible benefits from the state in the form of public goods, social safety nets, public works programs, etc. The issue is thus a political one of ensuring that throughout this reconstruction and building phase, that the public sector has sufficient resources that not only enables it to address the needs and services it has promised, but that it also has the flexibility to compensate for under-performance in some areas by offering further assistance in others. While state credibility/legitimacy will depend on performance in areas like basic security and the rule of law including tangible gains in combating corruption, sections of the population are undoubtedly going to judge the performance of the state in terms of whether it is having a measurable impact on their overall welfare in the short and medium term. This presents a serious challenge to the donor community, because the ceilings implicit in the notions of fiscal discipline may become dysfunctional for nation building, which in turn may have serious implications for long-term political and economic stability and development. So the parties need to be critical yet flexible when assessing what constitutes acceptable expenditure levels by the state.

As is well known, there are several factors that may create dilemmas for the fiscal ceilings. The first is that the cost of the Priority Reform and Reconstruction (PRR) pay reform is difficult to predict as it gets rolled out to all ministries and provinces. An important uncertainty here is what happens to the market for skilled labor over the coming years, as PRR pay scales will need to be adjusted in order to remain competitive. Here GOA is vulnerable to donor behavior, since the donors are without a doubt the "movers" of this critical labor market (see section 6.2.2 below).

There are a number of other strategic efforts whose costs can easily increase. One concerns the actual costs of the security sector, including demobilization and reintegration, and how fast these are to be incorporated into the budget. The public debt will increase. The anti-drugs activities and poppy-substitution efforts are to expand. Cost-recovery policies for key infrastructure investments (roads, water, energy, telecommunications) need to be put in place and enforced otherwise O&M costs will explode; etc. This is a daunting agenda for any country. For Afghanistan, which also has to rebuild basic structures, systems and services in a country that still has fragile communications and a series of fault lines in the national polity that constrain the options available, this needs to be borne in mind when deciding on assistance *levels* and *modalities*.

¹¹ It is not clear what share of total running costs of national security is included here. An Afghan National Army of 60-70,000 men may, according to some estimates, cost as much as USD 500 million a year. In addition come the police and other security-related sectors.

6.1.3 Recurrent Budget Funding and Policy Discussions

While the donors have so far provided funding to the budget under the ARTF Recurrent Window simply against fiduciary performance guarantees, the future seems to include more political concerns. One realistic concern is that less optimistic but plausible revenue- and expenditure scenarios may develop, so that the budget gaps may increase more than currently foreseen. The parties need to be realistic about the potential for such occurrences, and establish a mechanism that can address them.

The time seems therefore to have come for the authorities and donors to come together and discuss on a more permanent and in-depth basis the conditions for budget funding, and how to assess performance and agree on future targets. The fact is that the donors are today largely providing budget support, though through a common funding mechanism rather than directly to the Treasury. What is missing compared with more "classic" budget support funding, is the policy forum that goes along with it.

Such a policy forum should not be an integral part of the ARTF, however, but rather a mechanism alongside (though closely linked with) the ARTF. The reason is that the ARTF was established and structured as a funding mechanism. Using the ARTF set-up, such as the Donors Committee, as the policy forum would be problematic, for several reasons. The first is that such a policy forum might discuss larger macro-economic and budget issues, while the ARTF's mandate is simply to provide funding. But the most important reason is that the ARTF is a donor entity, whereas the policy forum should be driven and managed by the national authorities. A Macro-economic or a National Development Strategy Consultative Group (NDS-CG) would presumably be the best approach. A typical example of where such a forum would be useful, is the open letter to the GOA signed by eight important financing partners early 2005, where a number of questions are addressed to the new government. A NDS-CG that meets on a regular basis would provide a constructive setting for discussing and following up these and other issues of concern to the parties¹².

The ARTF should also strive for more longer-term commitments. The ARTF has so far succeeded in providing the necessary funding to the budget on a year-by-year basis. This "hand-to-mouth" funding is not in line with the medium-term funding framework most budget support arrangements are now putting in place. The ARTF should move towards a three-year rolling funding horizon where donors provide pluri-annual commitments. Along with increased predictability, donors may also consider more flexibility: when targets are met, this could be rewarded with additional funds being untied and passed through the ARTF. When targets are not met due to poor

¹² Exactly how such a policy forum should be structured, this Mission is not in a position to say. Some issues need to be taken into account. First of all, it needs to be GOA driven, and therefore respond to the kinds of policy concerns and priorities that are of greatest help to the authorities. Secondly, it should not overlap with or contradict existing efforts, so if it can fit into the current Consultative Group structure this would be helpful. Third, it needs to be mission focused: the forum is to deliver value-added to the actors. Whether it should focus on macro-economic issues or national development strategy depends on what GOA sees as useful, but also what is "topical" now. The PRSP is still some ways off, while the IMF's Staff-Monitored Program, recurrent budget funding gaps within the context of a Medium-Term Expenditure Framework or similar may be more urgent. Or it may be a wider public sector strategic development in the context of the Public Administration Reform and Economic Management (PAREM). What is important is that there is consensus around a "deliverables" program, and that the structure is then such that GOA and donors together can realistically produce these expected results.

government performance budget support may be reduced, but if it is due to exogenous factors, the NDS-CG would assess how to address this, find mutually acceptable solutions, adjust performance targets, etc.

This would contribute to strengthening the dialogue between the parties, build trust and commitments, strengthen information flows and thus avoid misunderstandings which typically arise at some stage under the kinds of complex circumstances that Afghanistan will be facing for some time to come. This will at the same time be in line with the Mutual Accountability-concern in the Paris Declaration (see Box 1), where donors would make themselves more transparent and accountable, thus reducing uncertainty and long-term transaction costs to GOA.

6.2 Investment Window Challenges

The Investment Window has been mentioned by a number of donors as "the future" of the ARTF, as they see it. The idea is that the government should assume responsibility for running core services as quickly as possible, while donors will provide the additional resources required for further expanding and improving public investments and creating the enabling environment for private sector development.

But the recurrent budget – personnel costs and operations and maintenance of existing and future public assets – ought to remain the funding priority for the donors. If the Ministry of Education does not have resources to pay the existing teachers, it makes limited sense to build more schools. If there is not sustainable funding in place for maintaining the existing trunk roads (whether through a cost-recovery mechanism or direct budget transfers or a combination), expanding the road network further only means that maintenance resources will be stretched even thinner, threatening the long-term viability of the existing infrastructure.

Since there is a reasonable expectation that the recurrent budget gap will increase over the short run, donors will have to increase their general ARTF funding considerably if they also want to see an increase in the level of investment window activities. While this may happen, a pragmatic expectation for the coming three-year period may be that donor funding may increase, but not much beyond what the increasing recurrent budget gap will require. Resources left over for investments will thus remain limited. If this is the baseline expectation, it may make sense to look at where ARTF funds can make the greatest difference.

The starting point is the observation that ARTF-funded activities have not followed any particular pattern or generated any particular synergies in implementation. They have rather been able to hang onto the coat-tails of KfW and IDA in terms of project development and technical management, but without having any pro-active criteria resulting from an analysis of what the comparative advantage of ARTF funding may represent to the country.

There are two dimensions this Mission would like to raise for consideration in this connection. The first concerns the ARTF as a mechanism for reducing overall transaction costs for accessing donor funding, and the other is whether the Investment and Recurrent Windows of the ARTF can generate synergies.

6.2.1 Aid Coordination Costs

What characterizes the ARTF is that it is a funding coordination mechanism where the World Bank as administrator has assumed a lot of the total costs of managing the

funds. This includes monitoring financial and results performance, assisting in disbursing resources, reporting back to the funding partners, engaging in dialogue with the authorities to resolve problems and carry out forward planning, carrying out various forms of quality assurance, etc.

From other work done on aid coordination/aid effectiveness, one "lesson learned" is that aid coordination costs are typically the least when it comes to credit-based activities and the greatest when it comes to technical assistance (TA).

Coordinating Credits

Credits typically are large lump-sums, they entail formal yet standardized agreements where the resources are registered at least on a country's debt management system but may also enter planning/budget systems since the resources are made available to the national authorities directly. Credits are typically used for large-scale infrastructure activities which in addition are the easiest to monitor in terms of performance: there is a direct link between funding and outputs produced which are easily verifiable and where there are international standards available for benchmarking purposes.

Coordinating Grants-funded Projects

Grants-funded activities are a lot "messier": donors provide them through a variety of mechanisms and modalities but typically the resources are made available for specific projects; the project agreements are sometimes through coordinating entities but often directly with line ministries, or through implementation by NGOs or private firms, often from the donor country; the donors have often been important in designing the project; disbursements may be handled from the field or from head office, etc. In short, donors manage the overall design and flow of funds, and it always becomes a challenge for national authorities to get a good picture of (i) financial commitments, (ii) actual disbursements, by fiscal year and project component, (iii) actual implementation of activities and where they are located geographically and in terms of relations to other sector or area activities, etc. In the case of Afghanistan, the MOF has to spend considerable resources keeping the DAD updated. The reconciliation with line ministries never provides the same information as that given by the donors, in part because neither donors nor line ministries really have much incentive to produce the kind of information in the format that is most helpful to the MOF.

Coordinating Technical Assistance

TA is difficult to coordinate for several reasons. One is that much of it is provided directly by the donors "in kind": consultants from the donor country hired and paid directly from the home office, often with the terms of reference (TOR) partly or largely developed by the donor. The problem with this is that different donors have quite different procedures for procuring TA services, the degree of professionalism in developing TORs and quality assuring the procurement varies; donor-specific characteristics mean TA services can vary considerably in approach; etc.

There is also a tendency to overload TA with three different kinds of tasks: (i) development and implementation of new systems and processes, (ii) delivering specific outputs related to these new systems – often having a management responsibility and being held directly accountable for these "deliverables", (iii) training of counterparts in using and taking over the new systems.

There are at least four kinds of problems that typically arise in these cases:

- The individual experts and even the TA team usually do not have the background/s to handle these three tasks simultaneously since they require different skills sets. In most cases, TA personnel are hired for their technical skills, not their training background and pedagogical experience.
- Given the time constraints that the TA personnel work under, and the conditions under which their counterparts often have to work, focus tends to be on the first two tasks – which are the most easy to monitor, tend to be the best specified in the contracts and thus the ones their performance is primarily measured against. Building the local capacity therefore tends to be given secondary importance, and hence lags.
- Training, mentoring, skills upgrading should be done on a broader basis than the project-specific outputs. This requires good coordination, preferably a sector or organization-specific capacity development strategy and action plan. These are often missing or are poorly specified, leading to task-specific training for identified counterparts rather than a more broad-based and forward-looking human resources development program that looks at systems-needs, career path development and beyond the particular department or ministry. The wastage of highly paid training/mentoring resources can therefore be quite high, while at the same time the TA attracts and retains much of the local skills that are available as counter-parts, thus creating rigidities within overall local HR management.
- Finally, the timeline for the different tasks are different. While implementation and first-round delivery can be done within a limited time period, capacity development takes time. Yet the TA contracts are structured to address the first issues, and capacity development therefore gets under-funded and tends to get cut well before the task has been done.

According to some estimates, donors spend about USD 400 million per year on TA. This is an enormous resource which is addressing critical constraints to the country's development: the limited capacity to plan, implement, quality assure and improve activities – in the public, private and NGO sectors, and at virtually all levels. "Getting it right" is thus of strategic importance.

6.2.2 The Labor Market for Skilled Labor

The key to addressing this issue is the labor market for skilled labor. Skilled labor is typically the scarcest resource in poor countries, and is recognized as such with a lot of attention given to capacity development and TA. The paradox is that donors tend to fragment and distort this market, creating severe problems for partner countries' development. In the context of the ARTF, there are three dimensions that merit attention: the demand for skilled labor in the public sector, the supply of skilled labor nationally, and the role that TA plays both regarding supply and demand. This labor market analysis needs to be situated within a more general public sector capacity development (CD) context, which typically comprises three levels.

- *Institutional development* addresses the overarching structure of the public sector, its size, the relationship to the private sector and civil society, the roles and relations between key public sector actors etc. Many of these questions are addressed in SAF, and the new government recently restructured its overall organization, for example.

- *Organizational development* is more directly relevant to labor market concerns. Functional analyses and other analytical tools help define core tasks, ministerial organigrams, the relationship to lower-level administrative units etc. This identifies what kinds of skills are needed, in what numbers, and where, in the sector. The PRR processes, for example, has produced improved organizational structure and focus, and better platforms for HR development.
- *HR development* addresses how to ensure that current staff acquire necessary skills, that new staff recruited has the requisite background, and performance is measured against clear goals, etc. A more complete HR framework would include career paths, job descriptions and hiring criteria that flow from the functional analyses/organizational development work. And it is the labor market that mediates between what the public sector wants and what it is able to acquire.

Demand for Skilled Labor in the Public Sector

As noted in chapter 5, Afghanistan is using ARTF-funding to improve the public sector's access to national skilled labor. The AEP is to recruit expatriate Afghans to provide senior policy advice for a very short period of time. The LEP will recruit manager and senior technical staff for time limited periods into line positions. These staff, if they perform well, can get more permanent positions through the PRR and PRR-Super Scale terms. The PRR is in part funded through the Recurrent Window.

The wage scales used in these three recruitment schemes are linked and seen as consistent. By recruiting new staff against clear job descriptions with specified salary scales, Afghanistan has put in place a structured, transparent and competitive public sector pay policy. This is a major achievement, as the country within a very short period of time has put in place a key component of public sector reform that many other countries have spent a decade working on and still do not have.

Supply of Skilled Labor

The supply of skilled labor for the public sector can come from in-house training, either by formal training institutions (several ministries have or are setting up their own training centers) or through on-the-job learning and mentoring (which is largely what TA projects provide); from technical and tertiary training institutions (Kabul University can be expected to play a particularly important role here); and from Afghans who have lived abroad and acquired relevant skills there. Over time, the first two sources will be the most important in terms of delivering permanent capacity.

While the demand side is now reasonably transparent, the public sector does not yet have a good supply side strategy in place. Such a strategy needs to look both at short-term skills upgrading and longer-term qualifications development.

Short-term training typically provides technical skills that are job-specific. This is usually managed "in-house": the institution specifies the needs, and either provides direct on-the-job training (often TA project-funded) or formal courses run by its own training centers, or contracts the training to be done by an external institution.

"Qualifications development" provides more generic skills in fields like accountancy, project planning etc. In some countries, these often form the basis for technical cadres who fulfill similar functions across ministries and see their careers move them around, in part providing the flexibility that is required for more effective public sector HR management. This training provides formal certificates and degrees from general

education institutions (university or polytechnics), while in a number of countries authorities have also established a public administration institute.

Afghanistan clearly needs a program of both general qualifications development, and skills training. The key decision lies in how the authorities intend to put in place a sustainable CD capacity – the ability to continuously supply the requisite skills in-country. This might involve a balance between within-ministry training centers, public administration institutes, and general training institutions, where the costs and benefits of the alternatives need to be assessed against different funding models and the capacity constraints that these various training institutions themselves face.

The work that is required to develop such a skills supply strategy involves a wide range of actors on both the government and donors (funding) side. Because the supply of key technical skills is fundamental to further improvement in overall PFM, and experience shows that close coordination is necessary if an efficient and effective solution set is going to be possible, joint donor action is helpful. The ARTF has so far not been directly involved in this area, but the parties could discuss if this would be an interesting option for the future, since most of the funders of training and technical assistance are already channeling funds through the ARTF.

TA and the Labor Market

Technical assistance projects affect the skilled labor market on both the supply and demand side. On the supply side, TA projects are injecting a considerable number of highly skilled personnel into technical and managerial positions ("gap filling" – substituting for lack of locally available skills), while also providing training and other forms of HR development among Afghani staff.

On the demand side, the TA projects tend to compete for skilled Afghani staff as counterparts, some projects hiring or at least paying hundreds of Afghanis who are recruited under better remuneration packages than standard civil service contracts.

The donors' influence on the job market is severe, because in addition to the TA projects, donors fund a large number of NGOs and private firms who carry out jobs under grants-funded contracts. These entities all are under pressure to "deliver", and efficiency concerns (producing outputs as quickly as possible) tend to override effectiveness issues (building local capacity to run and reproduce outputs). This is in part because of the short-time horizon of most contracts, in part because contracts often are poorly formulated and tracked regarding longer-term effects. Since many budgets are simply cost-plus based, the incentives to hire best skills available are high. This creates rent-seeking behavior on the side of local skilled personnel, and with donors and donor-funded implementers usually having poor information on the local labor market, they experience the skills scarcity as probably greater than it is. They thus both reinforce market segmentation and contribute to continuous upwards wage-ratcheting. Unless this is forcefully addressed, this will put increasing pressure on the PRR and PRR Super Scale rates, weakening the public sector's ability to attract key skills required for improved PFM – which the donors demand as a condition for further untying of aid.

The big advantage Afghanistan may have created for itself is that the pay-scale that is being put in place through the AEP-LEP-PRR program gives the market valuable information about what the public sector believes is fair compensation for a wide range of skills. Donors – and those who depend on donor funding for their activities – should be challenged to assess the job descriptions they are hiring for, and see if

wages paid compared with the responsibilities staff in the public sector have, is fair. One donor has evidently already carried out such an exercise, leading to decrease in pay for a number of its local staff as a result.

The problem is that it is not only the public sector, but also the nascent private sector that is being deprived of local skills when donor-funded activities bid them away. The long-term imbalance in the labor market can clearly only be addressed through an aggressive supply side response, but that requires considerable funding and will take time. In the mean time, if donor poaching of skills continues, Afghanistan's efforts at building its own capacities will clearly suffer.

The TAFSU project is providing some steps in the right direction. It is buying TA skills for the line ministries, and is using open tendering including in the region to find the most cost-effective skills for the different tasks. One thing is that this may bring TA costs down. Furthermore, since the TA contracts are handled by the national authorities, to the extent that the contracts include the hiring of local skills, this can be done at salary levels that do not distort the local labor market. By having the TA contracts handled by a national entity (the ARDS), this should ensure better definition of what kinds of TA should be given priority. This should make the overall size, focus and costs of TA activities more in line with GOA priorities¹³.

6.3 Recurrent and Investment Window Synergies

Chapter 4 noted that key PFM systems are largely in place, that early achievements are considered good, and are moving in the right direction. At the same time there is recognition that there is a lack of own capacity to manage, develop, quality assure and correct problems. This concerns the recurrent budget but even more the overall PFM cycle, which includes public sector planning and its integration into medium-term financial planning and management. High levels of public sector investments will continue in the years to come as will the need for market management since the private sector remains weak in many fields. But this means that public finance management capacity development (PFM-CD) linked with governance concerns will remain a key need for a considerable time to come.

The ARTF has proven to be an efficient and effective funding coordination vehicle for the recurrent budget. The Investment Window could in a similar way become a pooled fund for more programmatic allocations. One possibility is that it focus on *complementing* the Recurrent Window by funding a program in the field of PFM-CD. A basis already exists with the projects on the skilled labor *demand* side (AEP, LEP) and the funding through the recurrent budget for the PRR. The CCFO project and even more TAFSU provide first steps on the skilled labor *supply* and TA *management* sides.

With a more comprehensive and longer-term perspective, the ARTF can mobilize sufficient funds to provide the authorities with the means for a medium-term PFM-CD program. For such a program to be successful, a PFM CD policy and action plan need to be developed. This GOA could do with funding through TAFSU, for example.

¹³ This requires that the ARDS has a clear idea of what the priority needs are, and also is able to professionally manage TAFSU. Having a good working relation with the donor community will also be helpful since much TA will continue to come directly from the donors. Though ARDS should perhaps not be a TA coordinator directly, it can act as a "gateway" for TA information, and be a GOA instrument for TA management.

Since a number of PFM-CD activities no doubt will continue to be funded outside the ARTF, the coordination and policy development issues could perhaps become part of the agenda for the suggested policy forum.

Within such a program, the ARTF should concentrate on the TA activities and other "soft" dimensions such as scholarship programs (for training-of-trainers abroad or in-country, etc). Capital-intensive components such as building or rehabilitating training centers, larger equipment procurement etc. could be handled in parallel but outside the ARTF. This model would have several advantages:

- The PFM-CD program would give coherence and clear priorities to the ARTF Investment Window.
- It would provide badly needed resources for strengthening Afghanistan's PFM systems further, thus accelerating the country's ability to attract untied aid and over time move towards direct budgetary support.
- By using ARTF resources, the authorities can ensure comprehensiveness, coherence and a longer-term perspective on their efforts, ensuring increased effectiveness, relevance and sustainability.
- Untied and pooled ARTF funds improve efficiency on procurement, management and expert contracts, reducing transaction costs substantially in the field where such costs tend to be the highest. This includes reducing difference in TA approaches since they are procured by the same buyer, cutting the uncertainty that comes with having to negotiate extensions, revisions or exit strategies on the many donor projects that all follow different cycles, etc.
- Finally, since the TA contracts are formulated and owned by the authorities, GOA can demand performance, oversee, and – if need be – fire individual experts and firms much easier, which is an important issue since such contracts are costly.

6.4 Future Timeline for ARTF

Sooner or later the ARTF will be unnecessary. What should be the "sunset criteria"?

The first one is when there is no longer need for funding for the recurrent budget, since this has been the primary objective for the ARTF.

The second would be when there is also no value-added to the ARTF as a coordination mechanism for investment activities.

Over time, however, the distinctions between these two dimensions of the ARTF will become less meaningful. This will happen when Afghanistan begins to integrate its capital and recurrent activities and thus puts in place a comprehensive medium-term public sector budget. At that moment, funds become quite fungible. As the country's PFM improves, the need for a donor-managed coordination mechanism (ARTF with an MA) may be unnecessary – donors should be able to provide direct budget. To get there, Afghanistan will probably have to pass through some phases, with full budget support likely only five to ten years from now.

A key step in this process will be the emergence of the country's first Poverty Reduction Strategy (PRS). Afghanistan is putting together an Interim PRS during SY 1384 (appropriately enough with some ARTF funding to support the process). This will serve as a stepping stone to a fully-fledged PRS later on. Once that is in place, the

country should have an integrated budget for those areas that are important for its poverty reduction-relevant segments of the public budget.

A national development plan is considerably larger than a PRSP, however, since capital intensive activities like major infrastructure will remain important but not part of the PRSP. But the recurrent cost-intensive parts of the budget – primary level social sector services, basic rural and peri-urban infrastructure, etc – will be included. So the PRS will be important for developing the kinds of comprehensive and forward looking integrated budgets that are a pre-requisite for more general budget support.

It is therefore possible to conceive the ARTF as passing through four phases:

- i. ***The emergency phase***: SY 1381-1383. Here focus was on the recurrent budget, and the investment window concentrated on funding urgent needs.
- ii. ***The PFM-CD phase***, SY 1384-1388? Recurrent budget remains the priority item in terms of funding, but the investment window is focusing on supporting the PFM-CD. An action plan with annual targets (both in terms of donor funding and GOA performance) is in place, GOA procures and manages most of the ARTF-funded TA through mechanisms like TAFSU, direct procurement, etc.
- iii. ***The PRS phase***, SY 138?-???: The complete PRS permits more untying of aid, the distinction between recurrent and investment activities is less important in many of the sectors of greatest interests to the donors, and GOA is therefore able to put forth larger programs for funding, rather than projects. Several donors will already be providing direct budget support rather than going through the ARTF.
- iv. ***The budget support transition phase***: PFM systems are in place that ensure that internationally acceptable fiduciary standards are being implemented, GOA has a national development plan and a PRS in place that have been agreed to with the donor community, and the funds are provided as untied and un-prioritized funding through the ARTF to maintain some independent quality assurance for those donors who still are not totally comfortable with direct budget support. As this group of donors and the level of funding decreases, a sunset date for the ARTF is agreed to.

These phases will overlap. Activities that have begun under one phase will of course continue. Projects that were accepted during the "emergency phase" will continue till they have been finalized. During the second phase, many donors will undoubtedly continue to want to give preference to community development/service delivery programs like the NSP and MISFA rather than public sector CD. Other activities than just PFM-CD related ones may also be initiated during the current phase if funds are available and the parties agree to this. So the phasing is meant as being indicative of what the focus could be – depending on what the authorities prefer.

In line with the positive experience of having a Monitoring Agent for the recurrent budget, the ARTF may consider a similar arrangement for a PFM-CD program. Two models (or a combination) can be considered. One is the straight MA contract with a relevant firm or institution of repute. The other is a Quality Assurance Group of high-level officials that visit Afghanistan on supervision missions two or three times a year, and who act as much as advisers to the government as supervisors on behalf of the donors. The latter model, given the challenges of PFM-CD, may require also a contracted and more permanent secretariat to be in place.

The two last phases suggested above will largely be determined by the speed with which the individual donors accept criteria and performance as the basis for further untying their own aid. The experience with carrying out joint assessments of PFM in other countries, for example, is that different donors draw different conclusions and thus take different decisions based on the same information. The reason is simply that the policy makers back at headquarters have different criteria – including different levels of risk acceptance – for structuring development cooperation budgets.

While some donors may move to some direct budget support almost right away, others may therefore delay till additional quality standards or criteria have been fulfilled. As long as the ARTF provides GOA and these donors with value-added services through the planning and oversight coordination functions, the ARTF therefore would seem to be a worthwhile vehicle to maintain.

6.5 Conclusions and Recommendations

The main *Findings* and *Conclusions* are the following:

- The recurrent cost challenge may remain longer than is currently foreseen, since the government will be facing major challenges on both the revenue raising and fiscal restraint sides. The donors need to be realistic about this and forward looking in terms of providing required untied funding for this.
- The Recurrent Window is *de facto* budget support, but there is no permanent forum where the policy issues surrounding budget support can be addressed.
- The Investment Window should focus on activities where untied pooled funds contribute the most to reducing overall transaction costs, and also identify areas where synergies can be established with the concerns of the recurrent window, namely weaknesses in PFM capacity.
- Afghanistan is putting in place a reasonably transparent and competitive public service salary scale for skilled labor, in part using ARTF funds both for the PRR and ARTF projects. This is a major achievement in the context of general public sector reform.
- These efforts are suffering from donor funding distorting the market for skilled labor, ratcheting up wages and attracting away from the national public and private sectors many of the best skilled nationals.
- The key imbalance in this market is due to poor supply of more and better skills. The efforts so far are uncoordinated, expensive, and without clear choices regarding the balance between on-the-job skills upgrading versus formal qualifications training, what training should be provided within-ministry and what should be procured from external institutions, whether the public sector should establish a public administration institute or rely exclusively on universities and other schooling institutions, etc.
- TA today is costly, usually not provided based on open competition, the contracts are not owned by GOA and there is thus little performance management and

control. Considerable savings can be generated through better structuring and procurement of TA¹⁴.

- As Afghanistan's public sector planning and budgeting becomes more medium-term and comprehensive, the difference between recurrent and investment activities becomes less important. As the country's PRS comes into place, more donors will be willing to provide general budget support directly to the Treasury. However, this point is still some years off.

Based on the above, the Evaluation Team's **Recommendations** are as follows:

- A GOA-led Policy Forum should be established to develop a more permanent policy dialogue alongside the ARTF. The scope/agenda and participation in the Forum needs to be decided among the parties.
- The Investment Window should pay particular attention over the coming period to PFM capacity building (CD), including GOA-managed TA procurement. This will generate synergies with the Recurrent Window while addressing the area where donor-funded activities generate the highest transaction costs, namely TA and capacity building. It will strengthen PFM and thus create conditions for untied budget support.
- The ARTF should be conceived of as passing through different phases: (i) the Emergency Phase, just ended, (ii) PFM-CD and TA management for the next five years or so, (iii) PRS funding phase once a credible PRS is in place (at which time the distinction between Recurrent and Investment Windows will largely be illusory), (iv) Budget Support Transition. As the conditions for direct budget support develop, the value-added of a donor-managed coordination mechanism like the ARTF will diminish. But for the time being, it provides important services for a number of donors, and as long as this is the case, it should be maintained, till a final sunset date is agreed to by the parties.

¹⁴ One should not be naïve on this point. Ensuring that quality criteria are specified and that the suppliers that promise delivery at lower costs in fact can provide this is important. One contract that was put out to tender is already being criticized for not delivering the quality of services that the previous supplier had.

Annex A: Terms of Reference

These Terms of Reference describe activities required for the full evaluation of the operations of the Afghanistan Reconstruction Trust Fund (ARTF) during the period of March 2002 – March 2004. The evaluation is being carried under the supervision of the ARTF Donors Committee on behalf of the ARTF Management Committee.

Background

The Afghanistan Reconstruction Trust Fund, a multi-donor trust fund supported by 24 donors, has become the main instrument of government to fund the recurrent budget. Total pledged contributions to the fund, up to the end of March 2004 reached \$610 million. The ARTF has become the main instrument for support to the Government's recurrent expenditures – funding such necessary costs as the salaries of teachers and health workers. The ARTF Program, while supporting the Government's recurring costs, is also used increasingly as a mechanism to fund priority investments in the Government's reconstruction program. Seven investment projects, covering work such as telecommunications, power, microfinance and emergency employment, have been approved for a total commitment of over US\$85 million (and a further US\$21 million supports the UNDP Police Project).

The ARTF is overseen by a Management Committee comprising representatives of the Asian Development Bank, the Islamic Development Bank, the United Nations Development Program, and the World Bank. The Management Committee is responsible for reviewing progress and for making key management decisions, including for the approval of investment projects proposed for ARTF financing. The World Bank is the Administrator of the fund, and it has employed a Monitoring Agent to assist in ensuring proper fiduciary management. ARTF is managed by a Team Leader located in Kabul who reports to the World Bank Country Director for Afghanistan in Washington, with a subsidiary reporting arrangement to the World Bank Country Manager in Kabul.

The ARTF Program comprises three components:

- Recurrent and Capital Costs (also referred to as “Running costs”)
- Investment Projects or Activities
- Afghan Expatriates and Training

ARTF Goals

The ARTF provides a mechanism for coordinated funding of reconstruction activities in line with agreed priorities of the Government. The ARTF is designed to:

- (i) promote transparency and accountability of reconstruction assistance
- (ii) help reinforce the national budget as the vehicle for promoting alignment of the reconstruction program with national objectives;
- (iii) reduce the burden on limited government capacity for the first few years of re-engagement, while promoting capacity building over time; and
- (iv) help fund the essential recurrent budgetary expenditures required for the government to function effectively.
- (v) Provide a convenient mechanism for donors to fund priority investments.

Overall objective of the Review

The overall objective of the current exercise is to evaluate the effectiveness and impact of ARTF operations over the past two years (March 2002 – March 2004). This assessment will be made in terms of: relevance, impact, effectiveness, efficiency, responsiveness, and the sustainable benefits of the Art's activities, and overall institutional arrangements. Each of these aspects of ARTF operations will be assessed for the period under consideration as follows:

- A. *Relevance (The extent to which the ARTF is suited to the priorities and policies of the beneficiaries, recipient, and donor)*
 - a. To what extent are the goals of the ARTF still valid?
 - b. Did ARTF have a comparative advantage in funding Government Programs, and if so, was it correctly defined and articulated?
 - c. How useful did ARTF activities compare to activities funded by Government income ?
 - d. Were the stated objectives of each ARTF operation commensurate with this comparative advantage, clearly defined in strategy documents and measurable?
 - e. Are the activities and outputs of the ARTF consistent with the intended impacts and effects?
 - f. Are the activities and outputs of the ARTF consistent with the overall goal ?
- B. *Effectiveness (A measure of the extent to which all ARTF funded projects attain their objectives)*
 - a. To what extent were the objectives achieved / are likely to be achieved?
 - b. Which activities were most effective in contributing to the achievement/non- achievement of their respective stated objectives, what were the characteristics of these activities and to what extent could they have been replicated in other annual work plans?
 - c. Has the funding of essential recurrent budget expenditures improved the Government's budget process?
 - d. Has ARTF funding improved the Government's capability to provide services nationwide?
 - e. To what extent has transparency and accountability increased?
- C. *Efficiency (A measure of the outputs -- qualitative and quantitative -- in relation to the inputs)*
 - a. To what extent were the impact and benefits arising from activities commensurate with the level of effort and resources expended?
 - b. What were the most efficient areas of operation for ARTF activities ?
 - c. Which activities (if any) were cost-efficient?
 - d. Were objectives achieved on time in each of the ARTF funded projects?
 - e. Was each project implemented in the most efficient way compared to alternatives?

- D. *Impact (The positive and negative changes produced by ARTF projects, directly or indirectly, intended or unintended)*
- a. What has happened as a result of each project within ARTF?
 - b. What real difference has each activity made to the beneficiaries?
 - c. How many people have been affected?
 - d. Were ARTF stated goals and each project's objectives met?
- E. *Institutional Arrangements (An assessment of the appropriateness and effectiveness of the partnerships and other institutional relationships in which ARTF engages)*
- a. How appropriate, effective, and efficient were the institutional and management arrangements of ARTF during this period?
 - b. What were the most effective relationships (and specifically partnerships) under which ARTF operated?
 - c. What is an accurate description of ARTF's institutional relationship with the Ministry of Finance as well as other Government ministries?
 - d. How cooperative was the Ministry of Finance's relationship with other Government ministries?
 - e. What were the advantages and disadvantages of ARTF's institutional relationship with the World Bank?
 - f. How appropriate and effective were ARTF's governance, organizational structure, and staffing profile in realizing a relevant, effective, and efficient business plan?
- F. *Sustainability (A measure of whether the benefits of ARTF are likely to continue after donor funding has been withdrawn)*
- a. To what extent will the benefits of a project continue after the project ends?
 - b. What are the major factors that influence the achievement/non-achievement of sustainability of the project? E.g., what were the lessons learned?
 - c. How has ARTF strengthened the state's other sources of income?
 - d. How much longer is the ARTF needed to assist capacity building before the Government can assert control over the administration of budget funding from donors?
- G. *Responsiveness to opportunity*
- a. How responsive is the program to opportunities and demands that arise from Government and clients?
 - b. Is the management, planning and financial structure flexible enough to allow the program to respond to demands as they arise?
 - c. Do the benefits of such responsiveness outweigh the inevitable delay or disruption to the planned program of work?
 - d. How highly valued is such responsiveness by the program's clients?
- H. *Finances*

- a. **Financial Sustainability:** Has the ARTF effectively raised funds in this period? Has it pursued the right type of funding? What can be done to improve the sustainability/efficiency of fundraising?
 - b. **Financial Management:** Has the ARTF managed its finances effectively and efficiently in this period? Do the task managers manage their budgets appropriately? What can be done to improve the situation?
 - c. **Impact of financial management and funding uncertainties upon program effectiveness:** How has the funding availability affected the ARTF's performance (e.g. have delays in available funds hurt performance? Are bilateral or multilateral funds more effective)?
- I. *Recommendations for the Future*
- a. What is the current reality of Afghanistan and how does it impact on ARTF operations;
 - b. What are the new needs and demands of ARTF clients and partners;
 - c. What are the most effective interventions (products, thematic areas, modes of operation, etc.) for ARTF with its given track record and comparative advantages;
 - d. What are the potential financing opportunities for ARTF services in the coming period; and
 - e. Are ARTF's mission, goals, and strategies still appropriate?

Purpose

ARTF management requires detailed inputs to this process from a team of independent experts in the sector. The consultancy team will carry out the evaluation exercise, whose objectives are described above, and will oversee a consultative process which will enable ARTF Management to make recommendations to the ARTF Management and Donors Committees.

Outputs

The consultancy would result in the development of:

- a. Criteria and evaluation indicators for assessing the relevance, effectiveness, efficiency and responsiveness of ARTF operations;
- b. Specific criteria or an approach for assessing the impact of ARTF activities relating to sector reform and strengthening;
- c. An assessment of performance of each project against the evaluation indicators in the period 2002-2004;
- d. An assessment of the effectiveness efficiency and responsiveness of the ARTF institutional arrangements in force in this period; and
- e. Recommendations for future strategic focus for ARTF.

Deliverables

The consultancy will have the following deliverables:

Draft Evaluation Report

The draft evaluation will form the basis for more detailed consultation at national level and will contain:

- i. Draft assessment of general performance against agreed indicators in the period 2002-2004;
- ii. Draft assessment of the general effectiveness and efficiency of the institutional arrangements in force in this period;
- iii. Proposal for case studies of each ARTF funded investment project to be completed during the rest of the assignment.
- iv. Preliminary assessment of the key issues relevant to ARTF strategy, as well as likely levels and sources of funding in the coming five-year period;
- v. Detailed work program for finalization of evaluation through meetings.

Final Evaluation Report

The final evaluation report will incorporate comments from donors, ARTF Management Committee and the ARTF Administrator.

Activities

Preliminary Evaluation

- i) Assemble and review current strategy document, annual business plans, monthly and quarterly progress reports, mission aide memoirs, documentation prepared for the ARTF Management Committee (MC), minutes of MC meetings, and any other relevant management documentation which is available. All available documentation will be made available by ARTF management.
- ii) Make a preliminary assessment of the internal consistency between the Government reconstruction strategy, annual development budget, and activities/products delivered and develop draft indicators for evaluation of the relevance, effectiveness, efficiency and responsiveness of ARTF operations, the institutional structure, and the impact of institutional reform activities.
- iii) Hold preliminary meetings/ phone conversations with ARTF management, key staff (past and present if appropriate), Donors and ARTF MC members.
- iv) Develop a list of key contacts (individuals and organizations) who will participate in the evaluation exercise.

Local consultations

- i) Prepare a draft work plan, in consultation with ARTF regional management staff, for the completion of a local consultations.
- ii) Hold detailed meetings (by phone if appropriate) with ARTF management, Government Counterparts and Donors to plan for local consultation meetings. Agree on a final work plan including timetable, and a list of key invitees and people/organizations who will be consulted at local, national and international level.
- iii) Prepare a program and background material for a local consultation meeting which will be organized by ARTF staff. This meeting will be attended by at least

one member of the consultant's team, at least one member of ARTF MC, Donors and ARTF staff.

- iv) Participate in consultation meetings. Contact and consult on an individual basis with key members of the Donors representative, Government Ministries, ARTF staff, and ARTF MC to assess quality and impact of interventions at local and national level.
- v) Analyze the activities and impacts of the ARTF over the past two years, taking into account relevance, effectiveness, impact, efficiency, responsiveness, institutional arrangements, and sustainability.
- vi) Analyze the current situation and key relevant issues which should shape ARTF future operations (issues would include, for example, the MDGs, current thinking on various sectors reform, the role of the private sector, etc).

Completion

- i) Assemble and review feedback on evaluation paper and write draft interim report for submission to ARTF MC for comment.
- ii) Review feedback on draft interim report. Incorporate comments into interim report for submission to ARTF Donor Committee for comment.
- iii) Incorporate Committee's comments into draft report for donor meeting.
- iv) Produce final version of the evaluation.

Staffing and Resources

Staffing

The firm will provide a review team consisting of two to three professionals exhibiting a range of skills. Specific skills of the team will constitute:

Team Leader/ Institutional Specialist

The team leader will be a specialist with at least fifteen years of experience in the area of Public Financing and Administration, with a focus on institutional issues, of which at least five years should be experience of working for, or closely partnering with, international organizations working in developing country contexts.

The team leader/ institutional specialist will:

- Lead the team, providing direction and oversight to the evaluation exercise
- Design and oversee the evaluation, including taking responsibility for planning regional travel, coordinating meetings with key informants and ensuring there is adequate liaison and coordination with ARTF project units
- Liaise directly with the ARTF Program Manager and keep him informed of the activities of the team.
- Take the lead in developing the indicators for assessing ARTF performance, particularly in the area of institutional reform
- Take the lead in evaluating the institutional arrangements within which ARTF operates, including its institutional positioning, governance, management, partnerships, financing, and staffing
- Provide oversight and continuity for the evaluation exercise

- Take lead responsibility for ensuring all reports are produced in time, and be available for review and discussion with ARTF Management members in the latter stages of the consultancy

Project Implementation Specialist

The Project Implementation specialist will have at least ten years of developing-country expertise in the area of improving service delivery to vulnerable/conflict affected communities and households. At least five years of this experience should be directly linked to the delivery of reconstruction assistance in a post conflict environment. This expertise may have been gained in the private sector, NGO, or public sector.

The Project Implementation specialist will:

- Participate as a full member of the team in the evaluation development
- Lead the evaluation of the investment project portfolio of ARTF work, including evaluation of products and activities, the development of appropriate indicators of success, and the development of a future strategy
- Take the lead in the project evaluation exercises.

ARTF Contributions

ARTF will provide significant inputs to the process of the evaluation exercise. These contributions include:

- Staff Time: up to 2 staff weeks of Country Office staff. Up to 4 weeks of Program Manager in Kabul and the Management Team in Washington, DC.
- Costs of any consultation meetings
- Costs associated with the participation of ARTF MC members, Donor Committee members, Government Counterparts and other partners in all consultations
- Rapid and timely input to draft reports produced by the team
- Costs of production of final evaluation document for formal distribution to ARTF partners and clients

Cost Estimate

The cost estimate should include the costs of consultant time, travel and associated expenses, communications, production of all reports (8 copies) and other expenses.

Payment will be made on a lump sum basis on the production of the following reports:

- Mobilization 30%
- Interim Report 40%
- Final Report 30%

Management

This consultancy will be coordinated by Pierre Romand-Heuyer, Team Leader, ARTF and supervised by ARTF Donors who will actively participate in the exercise, with input from the ARTF Management Committee.

Annex B: List of Informants

Government of Afghanistan Officials

Ministry of Finance

H.E., Dr. Anwar-ul-Haq Ahady, Minister
Mr. Asad S. Farhad, Deputy Minister, Revenue and Customs
Mr. Wahidullah Shahrani, Deputy Minister, Budget and Treasury
Mr. Mujeebullah Sulaimankhail, Director General of Treasury
Mr. Shahpoor Taqat, Head, Special Disbursement Unit
Mr. Jalil Ahmad, Special Project Manager

Ministry of Rural Rehabilitation and Development

H.E., Mr. Hanif Atmar, Minister

Ministry of Commerce

H.E., Mr. Amin Arsala, Minister and Special Adviser to the President

Ministry of Communications

Engr Hassam Baryali, Deputy Minister

Control and Audit Office

Mr. Mohammad Sharif, Auditor General
Mr. Shamsuldin Raheem, Director, Directorate for Central Budgetary Institutions
Mr. Ghulam Sarwar, Director, Directorate for Coordination and Collaboration
Mr. Said Amin, Director, Directorate for Internal Audits

Afghanistan Reconstruction and Development Services

Mr. Adib Farhadi, Head

Kabul Province

Visits to Qarabagh District CDCs and projects

Kapisa Province Officials

Department of Finance (Mustoufiat)

Mr. Mohammad Sharif, *Mustoufi*
Mr. Mohammad Shaman, Head, Payments Department
Mr. Hajji Mohammad, Head, Book-keeping

Department of Education

Mr. Mohamad Asef Farhad, Head

Parwan Province Officials

Department of Finance (Mustoufiat)

Mr. Mohammad Azim, Head, Accounting Department

Mr. Gholam Mostafa, Head, Revenue Department

Mr. Khajeh Hazrat, Head, Payments Department

Department of Education

Ms. Rohalah Sadat, Director

Visits to Bagram District CDCs

Former Public Officials

Dr. Ashraf Ghani, Chancellor, Kabul University, former Minister of Finance

Ms. Nargis Nehan, former Director General, Treasury Department, MOF

Ms. Seema Ghani, former Director General, Budget

ARTF Technical Assistance Personnel

Recurrent Cost Window

Ministry of Finance

Mr. Janis Platais, Treasury Adviser (International Monetary Fund)

Mr. Peter Muir, Project Manager, Emergency Public Administration Project
(BearingPoint/Australia)

Ms. Mary Venner, Budget Adviser (BearingPoint/USA – USAID project)

Mr. John Whiteman, Budget Adviser (Maxwell Stamp – DFID project)

Mr. Ian Holland, Development Budget Adviser, Project Manager (UNDP project)

Mr. Paul O'Brian, Adviser

Mr. M. Reza Ravaee, Resident Manager, Monitoring Agent (PWC Netherlands)

Mr. Armand van Ramshorst, Adviser, Monitoring Agent (PWC Netherlands)

Mr. Serjick Avanesi, Adviser, Monitoring Agent (PWC Netherlands)

Control and Audit Office

Mr. Phil Duncombe, Technical Adviser (PKF)

Afghan Expatriate and Training Project (AEP)

Mr. Manfred Profazi, Programme Manager, International Organization for Migration

Mr. Eklil Hakimi, Adviser, Vice President's Office, IARCSC

Emergency Telecommunications Project

Ms. Sultana Parvanta, Consultant, Ministry of Urban Development and Housing

Kabul Power Supply Project & Kabul Roads and Drainage Project

Mr. Martin Jenner, Director, KfW

National Emergency Employment Program

Mr Bas Athmer, Chief Technical Adviser, MRRD

Mr. Wahidullah "Azizi", Senior NEEP Manager, MRRD

Mr. Michael Gillman, Procurement Adviser, MRRD

Mr. Gary K. Helseth, Chief, Operational Support Unit, UNOPS.

National Solidarity Program

Mr. Andreas Schild, Team Leader, Oversight Consultancy Team (GTZ)

Mr. William Meddlemiss, Chief Financial Officer, Community Empowerment and Public Works Project (BearingPoint/USA)

Mr. Rob Wrobel, Kabul Regional Support Manager, Oversight Consultants

Mr. Szilard Friczka, Chief Technical Adviser, UN Habitat

Mr. Steve Mason, Programme Grant Manager, Aga Khan Foundation

Mr. Abdul Waheed Hamidi, Head of National Solidarity Program, MRRD

Mr. Mitesh Thakkar, Senior Consultant, Altai Consulting

Ms. Michelle Kendall, Assistant Country Director, CARE

Mr. M. Nader Taher, Rural Assistant Programme Manager, CARE

Microfinance Project

Mr. Steve MacQueen, Project Director

Mr. Olivier Massart, Deputy CEO, First Microfinance Bank, Afghanistan

Mr. Mohamed Jalaluddin Ahmed, Country Manager, BRAC Afghanistan

Mr. Ibrahim Biswas, Manager, BRAC Afghanistan Microfinance Program

Kabul Roads and Sewerage Project

Mr. John-Marc Le Pain, Kabul Municipality (consultant)

Financial Management Capacity Project

Mr. Stuart Kane, Director, CCFO program, MUDH (Maxwell Stamp)

Mr. Robert Flanagan, CCFO/Justice and others (Maxwell Stamp)

Mr. Paul Adolphson, CCFO/Education, Higher Education, others (Maxwell Stamp)

Other Informants, Afghanistan

Mr. Satyendra Prasad, Consultant, Poverty Reduction and Private Sector Development (DFID)

Mr. Andrew Wilder, Director, Afghanistan Research and Evaluation Unit (AREU)

Ms. Sarah Lister, Senior Researcher, AREU

Mr. James Putzel, Director, Development Research Centre and Crisis States Programme, London School of Economics and Political Science

Donor Officials, Afghanistan

Asian Development Bank

Mr. Allan Kelly, Deputy Country Director

Canada

Ms. Nipa Banerjee, Counsellor Development / Head of Aid

Denmark

Mr. Jens Haarlov, Minister Counsellor

Ms. Charlotte Olsen, Deputy Head of Mission

European Commission

Mr. Jean-François Cautain, Head of Sector, Operations

Mr. Alain Frimigacci, Public Administration Reform and Justice

Germany

Mr. Mirco Kreibich, First Secretary, Development Cooperation

Italy

Mr. Carlo Batori, Counsellor and Deputy Head of Mission

Netherlands

Ms. Mariana Noteboom, Deputy Head of Mission

Norway

Mr. Jan Erik Leikvang, Ambassador

Ms. Nina Schjelderup, First Secretary

Sweden

Mr. Jorgen Persson, First Secretary

United Kingdom (DFID)

Mr. Richard Hogg, Country Director

Mr. Andrew Clark, Country Economist

Mr. Habib Rab, Economic Adviser

United Nations Assistance Mission to Afghanistan

Ms. Aameera Haq, Deputy Special Representative and UN Resident Coordinator

United Nations Development Programme

Ms. Karen Jorgensen, Senior Deputy Country Director

United States (USAID)

Mr. Patrick Fine, Director

World Bank

Mr. Jean Mazurelle, Country Manager

Ms. Nancy Zhao, Operations Adviser

Ms. Cecilia Kennedy, Finance Analyst

Mr. Mir Ahmad Ahmad, Operations Officer, Agriculture and Rural Development

Ms. Sherezad J. Monami Latif, Education Specialist, Human Resources Development

Ms. Keiko Miwa, Education Specialist, Human Resources Development

Mr. Manuel Jean-Yves Sarlin, Consultant, ARTF

Mr. Mohammad Khalid Payenda, Operations Analyst, ARTF

Funding Agency Officials, Head Office

Canada

Mr. Blaine Marchand, Deputy Director, Planning, Asia Branch, CIDA

Ms. Janet Lam, Project Officer for ARTF, Asia Branch, CIDA

Denmark

Ms. Nanna Skumsager Skau, Asian Department

Finland

Mr. Miko Pyhala

International Monetary Fund (IMF)

Mr. Steve Symanski, Afghanistan Desk

Mr. Theo Thomas, Economist, Fiscal Affairs Department

Norway

Mr. Bjørn Johannessen, former Ambassador to Afghanistan, MFA

Ms. Nina Schjelderup, First Secretary, Embassy in Kabul

Ms. Grete Løchen, Asia Desk, MFA

Ms. Anne Glad Fredriksen, Asia Desk, MFA

Mr. Arve Ofstad, Norad

Portugal

Mr. Pedro Rodrigues da Silva, Asia Branch, MFA

Sweden (Sida)

Tomas Bergenholtz, Asia Department
Ola Sahlen, Infrastructure and Economic Cooperation

Switzerland (Swiss Development Cooperation)

Mr. Clavel,

United Kingdom, DFID

Mr. Andrew Clark, DFID Country Economist

United Nations Development Programme (UNDP)

Mr. Jean-Claude Rogivue, Chief, South and West Asia Division
Mr. Sayed Aqa, Head, Mine Action Unit, Bureau for Crisis Prevention and Mitigation
Mr. Yoshiyuki Oshima, Program Specialist, South and West Asia Division

United Nations Office for Projects Services (UNOPS)

Mr. Nigel Fisher, Executive Director

United States (US Treasury)

Mr. Anthony Marcus, Deputy Director, Office of Afghanistan and Iraq
Mr. Ashok Parameswaran, International Economist, Office of Afghanistan and Iraq

World Bank

Mr. Hadi **Abushakra**, Chief Counsel, Middle East, North Africa & South Asia Region
Mr. Anders **Bjorgung**, Former Administrator, ARTF, Finance & Private Sector Dept
Mr. Asger **Christensen**, Senior Operations Officer, Rural Development Sector Unit, South Asia Region
Mr. Stephane **Guimbert**, Economist, South Asia Region
Ms. Els **Hinderdael-Forger**, Regional Procurement Manager, South Asia Region
Mr. Nick **Manning**, Lead Public Sector Management Specialist,
Mr. Blanshard **Marke**, Division Manager, Financial Management and Disbursement Division, South Asia Region
Mr. Alastair J. **McKechnie**, Country Director/Afghanistan
Mr. Honore **Ndoko**, Chief Administrative Officer, South Asia Region
Mr. Kjell M. **Nordlander**, Consultant Trust Fund Administrator, Trust Fund Operations, Concessional Finance and Global Partnerships
Mr. John **Roome**, Operations Director, South Asia Region
Mr. Pedro **Sanchez**, Senior Energy Specialist, South Asia Energy and Infrastructure
Ms. Donna **Thompson**, Senior Financial Management Specialist, South Asia

Annex C: Documents Consulted

Government of Afghanistan

- National Development Framework, DRAFT. Kabul, April, 2002.
- Afghanistan: Rebuilding Our Nation – Afghanistan’s National Program for Reconstruction. Islamic Transitional State of Afghanistan. 2003.
- Joint Review of the Afghanistan Portfolio*. Transitional Islamic State of Afghanistan and the International Development Association. February, 2004.
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ARTF Management Committee Meeting, August 9, 2004.

ARTF Management Committee Meeting, September 13, 2004.

ARTF Management Committee Meeting, November 8, 2004.

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Financial Status as of October 1, 2003.

Financial Status as of November 1, 2003.

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Financial Status as of March 19, 2004

Financial Status as of April 20, 2004.

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Monitoring Agent Contract between the International Bank for Reconstruction and Development and PriceWaterhouse Coopers, Contract No. 7120828. July 15, 2002.

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Public Administration Capacity Building Project, Technical Annex. Report T-7641 AF, December 27, 2004.

Rehabilitation of Satellite Earth Station, Billing System and Transmission Links – Project Appraisal Document. World Bank, June 3, 2003.

World Bank (2003), *Transitional Islamic State of Afghanistan; Emergency Communications Development Project; Technical Annex. Report No. T7602.* World Bank, September 2003.

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Afghan Expatriate and Training Project:

Expert Services and Training, TF053940, Grant Agreement. May 13, 2002

A Program for Short-Term Capacity Injection to Central and Sub-national Administration, TF053940, Project Proposal. December 9, 2004.

Emergency Telecommunications Project:

Telecommunication Project, TF052475-AF. July 10, 2003.

ARTF Telecommunications Project: Over-Runs on Bids. World Bank, ARTF Administrator.

Improvement of Power Supply to Kabul:

Feasibility Study Facility Project, TF050970, Grant Agreement. March 8, 2003.

Improvement of Power Supply to Kabul project, TF052541, Grant Agreement. December 10, 2003.

Rehabilitation of the 100 MW Naghlu Hydropower Plant (AFG/03136), TF050970. December 8, 2004.

National Emergency Employment Program:

National Emergency Employment Program – Phase I, FT050973, Grant Agreement. March 14, 2003.

National Solidarity Program:

National Solidarity Project, TF053939, Project Proposal, 2004.

Assessment of NSP Facilitating Partners, Common Final Report. Altai Consulting, August 2004.

National Solidarity Project, TF053939, Grant Agreement. August 15, 2004.

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Memorandum of Agreement between Ministries of Education and Rural Rehabilitation and Development of the Transitional Islamic State of Afghanistan on Construction and Rehabilitation of Schools. World Bank, ARTF Administrator.

National Solidarity Program – Operations Manual. World Bank, ARTF Administrator.

Repair to Kabul Major Roads & Drainage System:

Kabul City Roads and Water Drainage System Project, TF052482-AF, Grant Agreement. November 8, 2003.

Microfinance Project:

Microfinance Support for Poverty Reduction, TF052452, Project Application. 2003.

Microfinance Fund Project, TF052081, Grant Agreement. June 4, 2003.

Strengthening the Financial Management Capacity of Government:

Strengthening the Financial Capacity of Government, Project Application.

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Strengthening the Financial Capacity Project, TF052735-AF, Grant Agreement. October 11, 2003.

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Afghanistan Reconstruction Trust Fund – Legal Note on Police-Related Activities, Office Memorandum OM2002-0172. March 28, 2002.

Police-Related Activities under the Afghanistan Reconstruction Trust Fund: Legal Opinion, Office Memorandum OM2002-0064. April 26, 2002.

Finance Police-Related Expenditure, TF050855, Grant Agreement. June 9, 2003.

World Bank Internal Documents

Annex A to Bank Policy (BP) 8.40 - Contents of a Technical Annex to the Memorandum and Recommendation of the President.

Bank Policy 8.50 - Emergency Recovery Assistance

Operation Policy 8.50

Bank Policy 14.40 - Trust Funds

Operation Policy 14.40 – Trust Funds

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Background on Civil Service Work, Draft 2. EC, World Bank and the Government of Afghanistan.

Annex D: Conversation Guide, Donor Head Offices

1. What were the main reasons for providing funding to the ARTF [explore if there were particular interest in funding the recurrent budget versus projects, for example]? What were criteria for deciding on the amounts you have provided?
2. How would you compare the ARTF with other trust funds your country has supported? What are particular strengths, what are the main short-comings?
3. Are the governance arrangements for the ARTF satisfactory? Is decision making regarding new activities good (selection criteria clear, responsibility for decisions clear, the hearing of opinions structured and open, etc)? Is reporting and in particular information on results attained good enough? Is transparency and accountability overall of the ARTF satisfactory? If not, what can be improved?
4. Should the ARTF take on a different role when it comes to coordination, policy discussions – if so, in what direction (more or less work in these areas, for example)?
5. Do you believe the ARTF is more appropriate as a funding vehicle for the recurrent budget, or for development projects? If there is a difference, how does this influence your views on the ARTF's future? Under what circumstances would you consider increasing your ARTF funding?
6. Finally, if you were to look 3 to 5 years down the road, what do you think the ARTF should look like? Should it expand its project portfolio, should there be an explicit exit strategy – in which directions should the ARTF move, and why?

Annex E: Conversation Guide, Field Work

Conversation Guide, ARTF Assessment

24 donors are providing funds for the Afghanistan Reconstruction Trust Fund, ARTF. The World Bank is the Administrator of the ARTF, and has commissioned an assessment of its performance as well as possible recommendations for how it can be improved. The team contracted to carry out this task would like to hear your opinion on the ARTF. Below are some of the issues they would like to raise, but they would also appreciate your views on other aspects of the ARTF that you think are important for doing an overall assessment.

1. General Issues for all Informants

Do you believe the goals of the ARTF remain valid? Is the ARTF a relevant and a suitable vehicle for donor support to the Government's development efforts?

What do you see as the strengths, and what are the short-comings of the ARTF? Have any of these changed/improved over time? What are the reasons for the changes?

Do you believe the ARTF is more appropriate as a funding vehicle for the recurrent budget, or for development projects? If there is a difference, what does it consist of?

When looking at projects funded by ARTF, are objectives well defined and in line with Government priorities? Are outputs and activities reasonable, and are expected results specified and easy/possible to monitor? Since most ARTF activities receive funding also from other sources (Government revenue, donor funds), in what areas do you believe that ARTF provides specific value-added?

Are the governance arrangements for the ARTF satisfactory? Is decision making regarding new activities good (selection criteria clear, responsibility for decisions clear, the hearing of opinions structured and open, etc)? Is reporting and in particular information on results attained good? Is transparency and accountability overall of the ARTF satisfactory? If not, what can be improved?

If you look 3 to 5 years down the road, what do you think the ARTF should look like? Should it expand its project portfolio, should there be an explicit exit strategy – in which directions should the ARTF move, and why?

2. Issues for Government Officials

How do you see the management and decision making structure of the ARTF? Is Afghanistan's voice being heard in the way it should?

Do you believe the ARTF is addressing Afghanistan's priority funding? Do you feel that Afghani views are appropriately included in the design and selection of projects for ARTF funding? If not, what should be improved?

Is the ARTF an efficient and effective mechanism for mobilizing donor funds for Afghanistan's development needs? What are its strengths, what are the short-comings?

Overall, what do you see as areas of strength of the ARTF compared with alternative funding models? What are weaknesses, and how should they be addressed?

3. Issues for Donors/Funding Agencies

How much of your country's funding will go through the ARTF in 2005? How much in 2003 and 2004? Is there a trend in level and share of your country's resources through the ARTF, and if so, what is it, and what are the reasons for it?

Are you happy with the funding profile of the ARTF in terms of recurrent versus project funding? Do you see a shift in this profile, and do you agree with it? Overall, do you think the ARTF is filling its funding "niche role" well or should it change – in which case in what direction?

Do you find the ARTF project profile appropriate? What changes, if any, would you like to see in the kinds of projects the ARTF funds, and why?

Are you satisfied with the reporting you get on how your country's funding is being applied? Are you satisfied with the fiduciary management of the funds? Is your head office raising

Has your head office raised any questions regarding the ARTF? If so, what were they? In general, how do you see your country's relations to the ARTF over the next couple of years? Under what circumstances would you consider increasing your ARTF funding?

4. Issues for Implementing Partners (NGOs, Private sector, Public institutions)

How did your organization become involved in ARTF-funded activities (through competition/bidding process, invited in, or relevant public institution)? Was it easy to find out about the possibility of becoming involved/get access to ARTF funds? Did you experience the process of becoming an ARTF partner as transparent and fair?

Compared with other donor programs, is the ARTF easier or more difficult to work with/for? Are administrative procedures difficult/reasonable/easy? Are financial and performance monitoring/reporting easier/more demanding than with other sources of funding? What are differences to other funding sources?

Overall, how would you rate the ARTF as a funding mechanism for the activities you are engaged in compared with alternative funding sources, or experiences from other countries?

5. Issues for Civil Society/Private Sector/Stakeholder/Beneficiary Informants

Do you believe the ARTF is addressing Afghanistan's priority needs in an appropriate manner? How does the project you are involved in contribute to the Government's strategy in the sector you are working in?

Is the ARTF encouraging transparency, accountability in terms of how activities are selected and implemented? Is your experience that ARTF funded activities benefit those it was intended to?

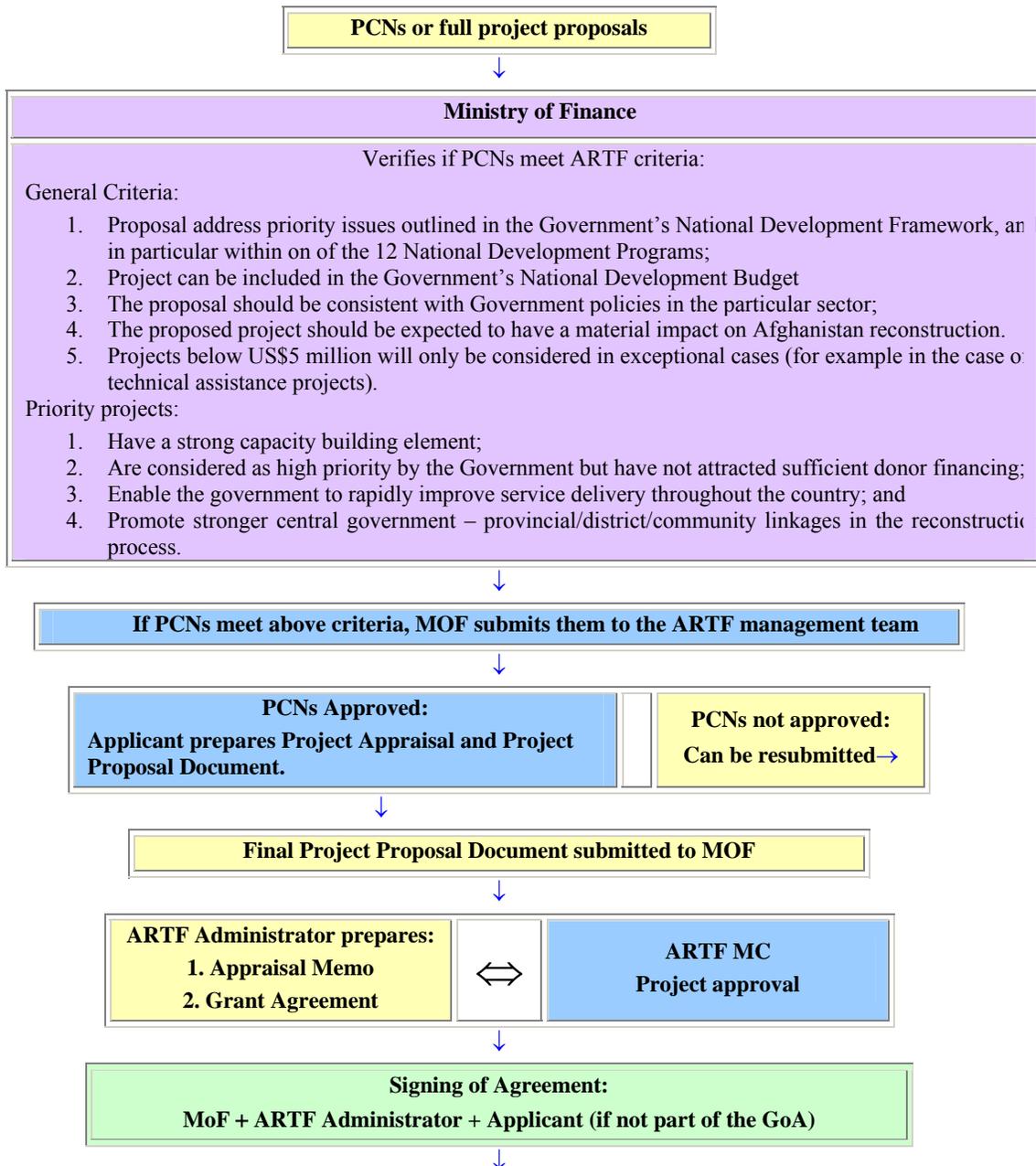
What is the level and form of involvement by relevant stakeholders in designing and selecting the activities ARTF funds? In what ways do you think this may affect effectiveness, sustainability, future impact of the activities?

A key "input" that international actors like the UN and World Bank can contribute, are as "knowledge centers" and understanding of "best practice" approaches. To what extent do you feel that the ARTF, with key "knowledge management" actors managing the fund, has contributed to strengthening project preparation, implementation and reporting, and how has your organization benefited and learned from this?

Overall, compared with other donor support to Afghanistan, what do you feel are the advantages and disadvantages of the ARTF? What are the positive and negative aspects of these kinds of donor-coordinated funding mechanisms?

Annex F: Process for submitting projects for ARTF funding

ARTF's Administrator's Internal Guidelines for Project Appraisal, Approval and Supervision provides guidelines regarding the cycle of ARTF's projects process from submission to approval, including appropriate channels and the partakers involved in the process. The Project Concept Note Template and Guidelines (PCN) is the ARTF proposal form submitted by the Applicant for funding. A PCN or a full project proposal is submitted directly to the MOF. The document *Guidelines to Applicants* provides guidelines to Applicants submitting requests for ARTF funding under the Investment and Program Component.



Open Project Special Account
Applicant is GoA: Account open by MoF
Other Applicants: Special Account opened by the Applicant at a Bank



Disbursements made by ARTF Administrator: Directly to the project's Special Account or makes direct payments to Providers contracted under the project, as specified in the Grant Agreement.



Quarterly progress reports from Applicant to the MOF and to ARTF management.

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World Bank (2000b): "Utilization of Project Implementation Units". Operations Evaluation Department, Lessons and Practices, No. 13. January 2