

# The Adaptation Fund

AFB/B.6/4  
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Adaptation Fund Board  
Sixth Meeting  
Bonn, June 15-17, 2009  
Agenda Item 7 (a)

## REPORT ON FIDUCIARY STANDARDS FOR IMPLEMENTING ENTITIES

## Table of Contents

1.	Note by the Secretariat.....	1
2.	<i>Adaptation Fund – Elaboration of Fiduciary Standards for Implementing Entities – Stage II.</i> Report prepared by CA Legal in association with Cambridge Economic Policy Associates Ltd.....	3
3.	Annex 1: Report of the Working Group on Fiduciary Standards.....	54
4.	Annex 2: Adaptation Fund – Fiduciary Standards - Outline Stage II Report.....	56

## Note by the Secretariat

1. At its fourth meeting, the Board *decided to create a working group [...] to accelerate the conclusion of fiduciary standards, including the consideration of the possible ways and means on how to implement those standards, through a specific study or any other mechanism with a view to making a presentation on this issue at the next meeting*<sup>1</sup>.
2. After hearing the report of the activities of the working group on fiduciary standards, the Board at its fifth meeting decided to:
  - (a) *Request the Secretariat to prepare a report on fiduciary standards and to incorporate that text into a revised Draft Provisional Operational Policies and Guidelines for Parties to Access Resources from the Adaptation Fund; and*
  - (b) *Request the working group on fiduciary standards, chaired by Mr. Julien Rencki (France, Annex I Parties), that had been established in Decision B.4/2, to continue to meet and to collaborate with the Secretariat in preparing the report on fiduciary standards mentioned in paragraph a above.*<sup>2</sup>
3. The mandate to the Secretariat to prepare the report on fiduciary standards<sup>3</sup> is attached to the present document as Annex 1.
4. The Secretariat hired the consultant firm CA Legal<sup>4</sup> to draft the requested report.
5. Due to time constraints and in consultation with the Board Chair and the members of the working group, it was agreed that the scope of the report would be restricted according to the proposal presented by the consultant, and cover the following items:
  - outline description of the accreditation process;
  - outline proposal on the nature of Secretariat services required by the Board in carrying out:
    - (i) the accreditation process; and
    - (ii) the process of approving proposals in the case of direct access;
  - outline proposal on mechanisms to assist Eligible Parties to access resources if their nominated national implementing entity does not fully meet the required fiduciary standards;

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<sup>1</sup> Decision B.4/2.

<sup>2</sup> Decision B.5/3.

<sup>3</sup> Report of the fifth meeting of the Adaptation Fund Board, Annex V.

<sup>4</sup> CA Legal is the author of the report on the elaboration of fiduciary standards for implementing entities submitted to the fourth meeting of the Board by the members from France and the UK (Annex I Parties) (See report of the fourth meeting of the Adaptation Fund Board, paragraph 33).

- outline proposal on arrangements for performance management and actions to be taken in cases of non-compliance (which would not have been fully tested against stakeholder policy concerns); and
- outline assessment of possibility of a phased/stepwise implementation of the proposed fiduciary standards system.

6. The outline of the above mentioned proposal is attached as Annex 2 to the present document.

7. The report *Adaptation Fund – Elaboration of Fiduciary Standards for Implementing Entities – Stage II* prepared by CA Legal is herewith presented for the consideration of the Board.

### **Recommendation**

8. The Board may wish to:

- (a) Note the report *Adaptation Fund – Elaboration of Fiduciary Standards for Implementing Entities – Stage II*;
- (b) Consider ways to include the content of the report as annex III of a revised *Provisional Operational Policies and Guidelines for Parties to Access Resources from the Adaptation Fund* and to make the necessary changes in its section *Accreditation for Implementing Entities* for consistency with the report.

**ADAPTATION FUND**

**ELABORATION OF FIDUCIARY STANDARDS FOR  
IMPLEMENTING ENTITIES - STAGE II**

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May 2009

Prepared by:

**CA Legal**

in association with

**Cambridge Economic Policy Associates Ltd**

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## LIST OF ACRONYMS AND ABBREVIATIONS

AF	Adaptation Fund
ARP	Accreditation Review Panel of the Adaptation Fund
Board	Adaptation Fund Board
CAL/CEPA Stage I Paper	CA Legal/CEPA paper entitled ‘Elaboration of Fiduciary Standards for Implementing Entities’ dated November 2008
CCM	Country Coordination Mechanism
CGIAR	Consultative Group on International Agricultural Research
CMP	Convention of the Parties
DAC	Development Assistance Committee
DFID	Department for International Development
EFC	Ethics and Finance Committee of the Adaptation Fund
FMA	Financial Management Assistance
GAVI	Global Alliance for Vaccines & Immunisation
GEF	Global Environment Facility
GF/Global Fund	The Global Fund to Fight AIDS, Tuberculosis and Malaria
IBRD	International Bank for Reconstruction & Development
LFA	Local Fund Agent(s)
M&E	Monitoring & Evaluation
MIE	Multilateral Implementing Entity
NIE	National Implementing Entity
PEFA	Public Expenditure & Financial Accountability
OECD	Organisation for Economic Cooperation & Development
Policies and Procedures	The ‘Provisional Operational Policies and Guidelines for Parties to Access Resources from the Adaptation Fund’ as drafted by the Secretariat and approved at the 5 <sup>th</sup> meeting of the Board
PR	Principal Recipient of the Global Fund

TAP	GAVI's Transparency & Accountability Policy
TOR	Terms of Reference
Secretariat	The Adaptation Fund Board Secretariat
SPPC	Strategic Projects and Programmes Committee of the Adaptation Fund
UNDP	United Nations Development Programme
UNFCCC	United Nations Framework Convention on Climate Change
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organization
WB	World Bank
WG	Working Group
WHO	World Health Organisation

## EXECUTIVE SUMMARY

### 1. Background

- 1.1. At the 4<sup>th</sup> meeting of the Adaptation Fund Board, a working group (WG) was created to look at ways to accelerate the selection by the Board of fiduciary standards for implementing entities<sup>5</sup>, including consideration of possible ways and means to implement those standards.
- 1.2. At its 5<sup>th</sup> meeting in March 2009, the Board adopted Policies and Procedures to operationalise direct access.
- 1.3. In April 2009, the Secretariat requested CA Legal/CEPA (building on their earlier report on the elaboration of fiduciary standards for direct access) to undertake a limited consultation with institutions with relevant experience of the management of “devolved relationships” to inform the preparation of an outline of a proposed system (taking into account the relevant elements of the Paris Declaration on Aid Effectiveness) to cover the following items:
  - an outline description of the accreditation process;
  - an outline proposal on the nature of Secretariat services required by the Board in carrying out:
    - (i) the accreditation process; and
    - (ii) the process of approving proposals in the case of direct access;
  - an outline proposal on mechanisms to assist eligible Parties to access resources if their nominated national implementing entity does not fully meet the required fiduciary standards;
  - an outline proposal on arrangements for performance management and actions to be taken in cases of non-compliance; and
  - an outline assessment of the possibility of a phased/stepwise implementation of the proposed fiduciary standards system.
- 1.4. In our earlier report we undertook a detailed desk review of the approaches adopted by other institutions that operate devolved relationships. For this report we undertook a further desk review, and conducted interviews with a Global Fund Local Fund Agent, a representative of the GAVI Alliance with responsibility for the GAVI Alliance’s

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<sup>5</sup> In our earlier report we gave a definition of project “implementation” (ie as opposed to execution) which includes project preparation, financial and other due diligence, allocation of funding, project management, and monitoring and evaluation.



Transparency and Accountability Policy (TAP), and representatives of UNDP, IBRD and the Multilateral Fund for the Implementation of the Montreal Protocol.<sup>6</sup>

1.5. We have made a number of assumptions in addressing the issues, as follows:

- it is likely that there will be one NIE for each AF eligible country, and that the entity will be a public sector entity close to the Ministry of Finance and Ministry of the Environment e.g. an agency of the Ministry of the Environment;
- that the Board will have the legal capacity to enter into such contracts as required to carry out the procedures proposed;
- the projects/programmes to which AF funding may be applied may vary widely in terms of many aspects, including: size; capital intensity; single/multidonor funding structure; technical complexity; local, national or regional focus; and responsible body within government.

1.6. Our report considers the nature of fiduciary standards (in the context of the systems adopted by other organisations); the nature of the accreditation process and how the accreditation process fits with the project approval process; an approach to performance management; and a number of implementation issues.

## **2. Fiduciary standards (in the context of the systems adopted by other organisations)**

2.1. This report includes a comparative analysis of the Global Fund, GAVI and the GEF. Significant differences exist between these organisations in a number of areas, for example, the variety and complexity of the projects that they fund, with the GEF funding the most complex projects; the coverage of the fiduciary standards (GAVI and Global Fund are purely financial whereas GEF includes institutional transparency); and the role of financial standards (e.g. Global Fund and GEF take a “pass or fail” approach whereas GAVI’s approach is informational to assist capacity building and select a funding mechanism). Also, the assessment itself is conducted differently: GAVI’s is undertaken by its Secretariat (i.e. in-house); at the Global Fund it is contracted out to “Local Fund Agents”; and GEF uses self –assessment.

2.2. We consider that, the range and technical complexity of the activities the AF is likely to encounter puts it in a context much closer to the Global Fund and GEF as the range of projects that the AF will fund will be greater. Given the different “ownership” context in which the AF will be established, there are, however, aspects of the GAVI approach (and

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<sup>6</sup> We were asked by certain WG members to specifically consider the approach adopted by the Multilateral Fund for the Implementation of the Montreal Protocol (the MF). However, the MF does not offer ‘direct access’, as envisaged by the AF, in the sense that it does not use national implementing agencies.

of direct budgetary support, to the extent that it uses information generated by PEFA) which are potentially relevant.

### **3. Fiduciary Standards**

3.1. We propose that the objectives (the Objectives) of the fiduciary standards should be to:

1. ensure that allocated moneys are applied for the purpose for which they are intended; and
2. ensure that funds are spent in as efficient manner as possible in order to maximise value for money.

3.2. We propose that the principles (the Principles) to be applied in relation to the implementation of these standards should be:

1. to apply fiduciary standards that meet the Objectives; and
2. to use existing country management systems and procedures to the extent that these are capable of achieving the Objectives; and
3. to transfer responsibility for implementation of projects and programmes to countries, and to monitor evaluate and review the performance of their implementation.

3.3. These Objectives and Principles are consistent with the principles and modalities agreed by the Conference of the Parties (Decision CMP5/CMP.2).

3.4. *Required competencies* that the NIE needs to demonstrate to meet the fiduciary standards are:

- I. Financial integrity
- II. Requisite institutional capacity
- III. Transparency and self - investigative powers

3.5. *The Specific capabilities* (i.e. the attributes which need to be demonstrated which underpin the required competencies) are:

#### I: Financial Integrity:

- *The ability to accurately and regularly record transactions and balances to an appropriate standard as attested to by a competent entity which can be illustrated by the production of regular, reliable financial statements, audited/externally scrutinised accounts, and the production of independently*

verified, detailed accounts, and the installation of internationally recognised accounting packages (e.g. SAGE).

- *The ability to safeguard, manage and disburse funds efficiently to recipients on a timely basis* which can be illustrated by financial projections demonstrating financial solvency and by the demonstration of proven payment systems.
- *The competency to produce forward-looking financial plans and budgets* which can be illustrated by evidence of preparation of corporate or departmental/ministry budgets and detailed analyses of previous outturns versus budgets.
- *Legal status to contract with AF and third parties.*

## II: Requisite Institutional Capacity

- *Procurement procedures which provide for transparent competition including effective means of redress* which can be illustrated by evidence of procurement policies and procedures consistent with best practice (ie transparency, competitive tendering)
- *Capacity to undertake monitoring and evaluation* which can be illustrated by the availability of resources to implement an agreed monitoring and evaluation framework, including the preparation of regular reliable programmatic reports, and the demonstration of ability to undertake systematic collection of relevant data for the purposes of evaluations and other studies.
- *Ability to identify, develop and appraise project – ex ante and ex post – technically, legally, financially, economically, socially and environmentally (as appropriate)* which can be illustrated by the availability of resources to conduct requisite ex-ante and ex-post appraisals of projects of a similar complexity.
- *Competency to manage or oversee the execution of the project including ability to manage sub-recipients, fit for purpose infrastructure and resource to support project delivery and implementation* which can be illustrated by comprehensive understanding of and capacity to address the technical, financial, economic, social, environmental and legal aspects of the project and their implications, and demonstrated competence to execute or oversee the execution of projects or programmes of the same nature as the intended projects or programmes.

## III: Transparency and Self - investigative Powers

- *Freedom to whistle-blow on issues of fraud and gross mismanagement* which can be illustrated by demonstration of a written policy and / “fraud hot-line”, and whistle-blower protection policies.
- *Objective policy for self-regulation* which can be illustrated by policies for maintaining accreditation and for addressing any problems as they arise.

- 3.6. These specific capabilities required to demonstrate the competencies for III (Transparency and Self - investigative Powers) are not capable of being outsourced or provided externally to an NIE.
- 3.7. The competencies and capabilities set out in II (Requisite Institutional Capacity) can only be assessed in the context of an individual project or programme proposal. This is because the competencies and capabilities for the project proposal stage will vary widely depending on the nature of the project. This means that these competencies and capabilities cannot be assessed in an absolute sense, they need to be considered relative to the implementation capability demands of the specific proposed project or programme, as these will vary tremendously.
- 3.8. It should be noted that procurement could be treated as a financial, rather than institutional, standard for the purposes of basic procurement, which means that following financial accreditation an NIE would be accredited for the purpose of undertaking basic procurement. For more complex procurements, appropriate institutional capability would be required.
- 3.9. The assessment of institutional capabilities (i.e. standards set out in II (Requisite Institutional Capacity) will be led by the Secretariat (possibly with specialist technical external support) in order to build up institutional learning of the capabilities of the different NIEs. This contrasts with financial accreditation where there will be a greater reliance on third party service providers.

#### **4. Financial Accreditation**

- 4.1. Eligible Parties will submit applications for accreditation of NIEs directly to the Board. The proposal will include a detailed self-assessment of how the NIE's own systems meet the fiduciary standards with appropriate relevant supporting documentation e.g. Public Expenditure and Financial Accountability (PEFA) reports etc.
- 4.2. The Board appoints an "Assessor" - a third party service provider appointed following a competitive process - which undertakes the assessment in two stages with an initial desk review followed by an in-country review. A member of the Secretariat could join the Assessor in conducting the review.
- 4.3. The assessment team submits its findings to an "Assessment Review Panel" (see below) which reviews the country proposal and submits a recommendation to the Board:
  - (i) that the NIE meets the fiduciary standards and should be accredited ("**Accreditation**"); or
  - (ii) that the NIE does not meet the fiduciary standards in all respects but may be reconsidered for accreditation if it addresses areas where it does not meet the fiduciary standards, through, for instance, relying on verifiable third party

capabilities in its areas of weaknesses (“**Conditional Accreditation**”); or

- (iii) that the NIE does not meet the fiduciary standards required, and is unlikely to do so even with third party assistance. In this case, the eligible Party would be required to access AF funding indirectly via an MIE, until it were able to put forward (either the same or a different) NIE able to obtain Accreditation or Conditional Accreditation (“**MIE Support**”).

- 4.4. In the case of Conditional Accreditation, the Board will require the Secretariat to consult with the NIE as to how third party support (including from an MIE or bilateral donor) might be utilised to address those areas where it has not met the fiduciary standards, both in the short term to allow initial projects to be funded, and in the longer term through capacity building with a view to allowing the NIE to meet the standards itself and to submit for full accreditation in due course. In each case, the question of how this will be funded will need to be considered and, if funding is to be made available by the AF, a process and parameters for accessing such funding will need to be established. It is suggested that countries be allowed to take responsibility for negotiating arrangements for such support, in order to allow coordination with existing initiatives.
- 4.5. An NIE may appeal against a decision of the Board.

## **5. Performance Management**

- 5.1. The Board through the Secretariat will undertake or commission from the Assessor a periodic (e.g. every 2 years) assessment report of the NIE’s performance against the fiduciary standards. The Board may also commission ad hoc special investigations where these are necessary.
- 5.2. If the Board determines that the NIE no longer meets the fiduciary standards the Board will request the Secretariat to confirm to the NIE that it is no longer accredited, and may re-submit for accreditation when it addresses the areas where it does not meet the fiduciary standards.
- 5.3. It is proposed that the Board should consider developing a risk management/early warning system to assist it in identifying projects/programmes that potentially give rise to a significant risk for example due to value, complexity and other factors.
- 5.4. The draft Policies and procedures make provision for the cancellation, termination and suspension of projects where financial irregularities are found. The Board may also consider terminating the accreditation of an NIE in such circumstances.

## **6. Implementation Issues**

- 6.1. The Board would establish an independent Accreditation Review Panel (ARP). The ARP would be made up of independent technical experts. The ARP would report to the Board.

The advantage of this approach over using the Strategic Projects and Programmes Committee is that the members of the panel would be independent. It would also free up time for Board members.

- 6.2. The Board should engage external service providers as Assessors to support the financial accreditation, and performance monitoring processes rather than conducting these reviews in house. The advantages of the use of external assessors over undertaking the role in house are that the service providers would bring their professional reputation, and independent specialist professional judgement, to bear. They would also have PI insurance.
- 6.3. The external service providers will be engaged through an international competitive process.
- 6.4. A detailed assessment of the work involved and therefore the cost of each accreditation and performance management review is outside the scope this report. However, our initial estimate is that each financial accreditation review, if undertaken by a third party service provider, would take between 15 to 35 person days, and cost between USD 30,000 to 70,000, depending of course on the complexity of the entity being reviewed.
- 6.5. Our initial estimate is that the NIE performance management reviews would take between 10 and 20 days, and cost between USD 20,000 and 40,000 depending on the complexity of the entity being reviewed.
- 6.6. Initially, fast-tracking is likely to apply to projects and programmes which are small-size (up to US\$1 million and technically simple). In future years, fast tracking may also be extended to cover projects/programmes where the NIE has been accredited for and successfully carried out a similar project/programme, or where the project is an extension of an existing project/programme.
- 6.7. It is noted that the proposals in this paper are required to be aligned, to the extent deemed possible and relevant, with the key principles of the Paris Declaration on Aid Effectiveness. In particular, country ownership, alignment and harmonisation are addressed by: the origination of proposals within country; the use of the NIEs' own procurement and PFM systems to the extent these meet the minimum fiduciary standards; where NIEs require support to meet the standards, the coordination with existing bilateral and multilateral initiatives; and the use, as part of the accreditation process, of existing reports and analysis.

# **I PURPOSE**

## **1.1 Background**

1.1.1 In November 2008, CA Legal/CEPA prepared a paper entitled ‘Elaboration of Fiduciary Standards for Implementing Entities’ (the CAL/CEPA Stage I Paper), which was presented at the 4<sup>th</sup> meeting of the Adaptation Fund (AF) Board (the Board). The purpose of the CAL/CEPA Stage I Paper was to describe a range of options that could provide eligible Parties<sup>7</sup> with “direct access”<sup>8</sup> to AF funding in ways that are compatible with international fiduciary standards<sup>9</sup>.

1.1.2 At the 4<sup>th</sup> meeting of the Board, a working group (WG) was created to look at ways to accelerate the selection by the Board of fiduciary standards for implementing entities, including consideration of possible ways and means to implement those standards. The Adaptation Fund Board Secretariat (the Secretariat) was mandated to draft the ‘Provisional Operational Policies and Guidelines for Parties to Access Resources from the Adaptation Fund’ (the Policies and Procedures), which would establish procedures to operationalise direct access. The Policies and Procedures (as subsequently amended) were adopted by the Board at its 5<sup>th</sup> meeting in March 2009.

1.1.3 The Policies and Procedures set out a system for direct access whereby eligible Parties may access AF funding either via National Implementing Entities (NIEs) (being national entities nominated by each eligible Party), or Multilateral Implementing Entities (MIEs) (being multilateral institutions and regional banks), which in each case must be recognized by the Board as meeting the fiduciary standards established by the Board and which will bear the full responsibility for the overall management of the projects and programmes financed by the AF, including all financial, monitoring and reporting responsibilities.

1.1.4 At its 5<sup>th</sup> meeting, the Board also mandated the Secretariat to prepare a report on fiduciary standards to inform and be incorporated into the Policies and Procedures. In April 2009, the Secretariat requested CA Legal/CEPA to provide a second report, looking at certain specific aspects of direct access and fiduciary standards, building on the CA Legal/CEPA Stage I Paper and the Policies and Procedures.

## **1.2 Scope**

1.2.1 Given the timescale for the work, some aspects of the TOR proposed by the Board could not be undertaken; namely: a detailed review of the approaches adopted by other

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<sup>7</sup> Developing country parties to the Kyoto Protocol who satisfy the AF’s eligibility criteria.

<sup>8</sup> As defined paragraph 29 in Decision 1/CMP.3 of the Third Conference of the Parties to the Kyoto Protocol.

<sup>9</sup> As required by decision 5CMP2.

institutions to fiduciary standards in the management of “devolved relationships”; a detailed proposal on specific fiduciary standards to be adopted; and a detailed assessment of the technical and financial implications of establishing proposed fiduciary standards. As such they are outside the scope of this paper.

1.2.2 The agreed TOR requires a limited consultation with institutions with relevant experience of the management of “devolved relationships” to inform the preparation of an outline of the proposed system to cover the following items:

- an outline description of the accreditation process;
- an outline proposal on the nature of Secretariat services required by the Board in carrying out:
  - (i) the accreditation process; and
  - (ii) the process of approving proposals in the case of direct access;
- an outline proposal on mechanisms to assist Eligible Parties to access resources if their nominated national implementing entity does not fully meet the required fiduciary standards;
- an outline proposal on arrangements for performance management and actions to be taken in cases of non-compliance; and
- an outline assessment of the possibility of a phased/stepwise implementation of the proposed fiduciary standards system.

1.2.3 We have noted the Board’s request to the Secretariat to take into account the relevant elements of the Paris Declaration on Aid Effectiveness in developing a system of fiduciary standards.

1.2.4 We have focused in particular on considering the nature of the accreditation process, how the accreditation process fits with the project approval process, and on proposing an overview of the nature of fiduciary standards to be assessed under each process (in the context of the systems adopted by other organisations, as described below).

### **1.3 Methodology**

1.3.1 In preparing this report we have consulted with members of the WG on a short paper which we prepared for discussion purposes. The key issues identified by members of the WG are set out in Appendix 2 to this paper.

1.3.2 In preparing the CAL/CEPA Stage I Paper, we undertook a desk review of the approaches adopted to fiduciary standards by the GAVI Alliance, the Global Fund, the



GEF, UK direct budgetary support, Cities Alliance, and CGIAR in the management of “devolved relationships”.

- 1.3.3 We have followed up on this work by undertaking a more detailed desk review of the approaches adopted by GAVI and the Global Fund in particular, and we have spoken to representatives of UNDP, IBRD, the Multilateral Fund for the Implementation of the Montreal Protocol, a Global Fund Local Fund Agent and a representative of the GAVI Alliance with responsibility for the GAVI Alliance’s Transparency and Accountability Policy (TAP). We have also drawn on our earlier desk review of UK direct budgetary support.
- 1.3.4 The findings of our desk review and limited consultation with GAVI and the Global Fund are set out in Appendix 1.

## **1.4 Structure of the report**

- 1.4.1 Following this introductory section, the paper is organised as follows:

- Section 2: Definitions and Assumptions

- Section 3: Putting Fiduciary Standards in Context

- Section 4: Fiduciary Standards

- Section 5: Financial Accreditation

- Section 6: Performance Management

- Section 7: Implementation Issues

## **Appendices**

Appendix 1 – GAVI and Global Fund approach to Fiduciary Standards and Devolved Management

Appendix 2 – Key Issues Arising from Consultation with the Working Group

## II DEFINITIONS AND ASSUMPTIONS

### *Definitions*

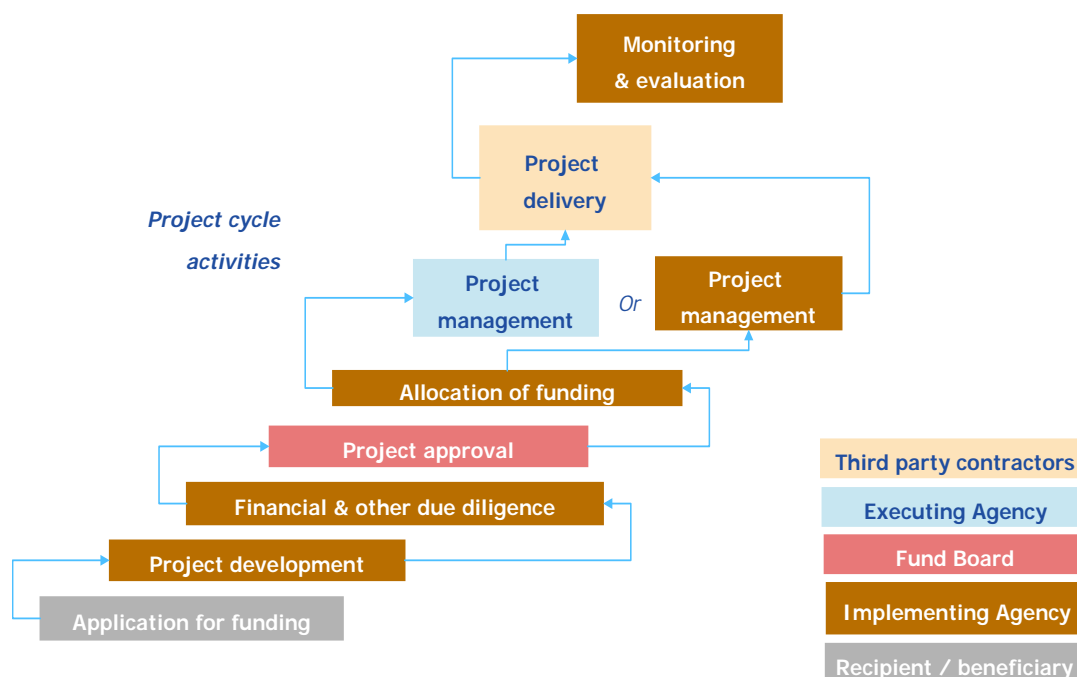
#### **2.1 Implementation and Execution**

2.1.1 In the CA Legal/CEPA Stage I paper we provided a definition of “Implementation” and “Execution Functions” for AF funded projects. Most of any NIE functions are around the implementing function, although it is possible that the NIE could be responsible for project execution, depending upon the circumstances. Typically the implementation entity role involves the following:

- *Project preparation*: the ability to identify and develop projects, in terms of its scope, development of contractor terms of reference etc.;
- *Financial and other due diligence*: the ability to ascertain the financial, technical, legal and other implications of the project or program;
- *Allocation of funding*; the accurate payment of contractors and other third parties on a timely basis;
- *Project management* (where the implementing entity also has an executing role): including the procurement and management of consultants, contractors and other advisors; and
- *Monitoring and evaluation*: ensuring that key project and program outputs, outcomes and impacts are appropriately captured, measured and assessed.

Figure 2.1 illustrates graphically, how these roles might fit into a typical AF project cycle.

Figure 2.1: AF project cycle



Although many recipient countries are relatively used to “executing” projects, fewer initiatives involve locally-based “implementation” activities.

### Assumptions

## 2.2 Number and status of National Implementing entities

- 2.2.1 We understand from our discussions with Board members that it is likely that there will be one NIE for each AF eligible country, and that the entity will be a public sector entity close to the Ministry of Finance and Ministry of the Environment e.g. an agency of the Ministry of the Environment.
- 2.2.2 If the NIE is a government ministry this could raise issues as to the Fund’s ability to require external audit of the ministry’s accounts, and consideration may need to be given as part of the accreditation process to the acceptability of reliance upon the country’s own national audit institutions. In this regard we understand that GAVI requires countries to manage the Health Systems Strengthening funds (cash support for children’s health services) in official government accounts that are auditable and subject to government financial management procedures. Countries are also required to submit annual external audit reports on their funds.

- 2.2.3 If the NIE is an agency of government rather than a ministry it is anticipated that the entity's accounts could be audited by an external agency. The use of agencies of government could also facilitate the NIE's ability to co-ordinate cross departmental activities. It could also enhance the NIE's ability to access technical expertise and resources across a range of areas. On the other hand if a new agency were created consideration would need to be given to ensuring that the creation of a new entity did not prejudice the co-ordination of the country's development efforts in this area.
- 2.2.6 The accreditation system and fiduciary standards that we have proposed could be applied to any NIE whether public or private sector. However, the choices made on the number and status of the NIEs will of course have a considerable bearing on the institutional, legal, technical and financial issues for the Board.
- 2.2.7 We understand that AF projects will include both national and regional projects with cross-border dimensions. The focus of this paper is on national implementing entities. Consideration will need to be given to the implementation of cross-border projects and the accreditation of regional implementing entities. The fiduciary standards and process for the accreditation of these entities should be consistent with the approach adopted by the AF for NIE's.

### **2.3 Legal capacity of Board to contract**

- 2.3.1 We note that in decision 1/CMP.4, paragraph 11, the CMP resolved that the Board be conferred such legal capacity as necessary for the discharge of its functions with regard to direct access by eligible Parties. This paper therefore assumes that this resolution has been implemented, and that the Board will have the capacity to enter into such contracts as required to carry out the procedures proposed in this paper (for example, the capacity to contract external consultants to carry out accreditation of NIEs under the accreditation process).

### **2.4 Scale and complexity of projects**

- 2.4.1 In proposing an accreditation process for implementing entities, it is necessary to consider the type and range of projects/programmes to which AF funding may be applied. We have assumed for this purpose that the projects/programmes to which AF funding may be applied may vary widely in terms of many aspects including: size; capital intensity; single/multidonor funding structure; technical complexity; local, national or regional focus and responsible body within government.

### III PUTTING FIDUCIARY STANDARDS IN CONTEXT

#### 3.1 Overview

3.1.1 In the CA Legal/CEPA Stage I report we undertook a desk review of a range of systems for the application of fiduciary standards to devolved management arrangements. In this Stage II we undertook a more detailed review with limited consultation of the approaches to the adoption of fiduciary standards by entities which have the most in common with the AF. In our view these are:

- The Global Fund which involves national implementing entities (Principal Recipients) disbursing funds for several uses associated with addressing the challenges of tuberculosis, HIV and malaria.
- GAVI which uses national implementing entities as conduits for the implementation of vaccination programmes.
- The GEF which has developed fiduciary standards to govern the use of its funds for a wide range of applications, typically by MIEs.

3.1.2 We were asked by certain WG members specifically to consider the approach adopted by the Multilateral Fund for the Implementation of the Montreal Protocol (the MF). The MF approach involves the use of ‘National Ozone Units’ in each relevant country, which act as national focal points for the Montreal Protocol. However, the MF does not offer ‘direct access’, as envisaged by the AF, in the sense that it does not use national implementing agencies. Instead, the MF has contracted the following multilateral entities (or their country offices) to act as implementing agencies: UNDP, UNEP, UNIDO and the World Bank, plus several bilateral agencies representing donor governments. In addition, the MF does not set out its own fiduciary standards, as it relies on those of its implementing agencies. This understanding was confirmed by a call with a representative of the MF. Therefore, it was decided not to focus in further detail on the MF approach. The same is true of UNDP, which, notwithstanding its modalities for national execution, has not adopted processes for national implementation, but instead tends to carry out the implementing role itself.

3.1.3 We have also not considered in detail bilateral forms of budgetary support (although the DFID model was examined for the purpose of the CA Legal/CEPA Stage I Report). This is for two principal reasons: (i) we believe that budgetary support is much less project/programme specific (in contrast to our understanding of the AF) and therefore focuses on financial management capabilities rather than also institutional/technical capabilities; and (ii) budgetary support, as a bilateral process, tends to focus less on objective ‘pass/fail’ fiduciary standards, and more on identifying areas of risk, after

which a judgment call can be made by the donor. For a multiparty fund such as the AF, we would argue that a more deterministic process is required.

3.1.4 It is important to note that there are significant differences between the contexts within which these other organisations operate and that within which the AF will operate. For example, for GAVI and the Global Fund, whilst their work in health systems strengthening potentially involves a wide range of implementation activities, the performance management for much of their immunisation work can be achieved through ensuring that countries operate effective “data quality management”. GAVI’s experience of performance management of technical aspects of implementation is therefore of limited relevance to the Adaptation Fund. GAVI also has access to considerable technical resources through its alliance with the WHO and UNICEF.

3.1.5 Table 2.1 provides a high level summary comparison of some of the key similarities and differences between these entities’ approaches to fiduciary risk management.

*Table 2.1: Comparison of key aspects of the fiduciary standards.*

	<b>Organisation</b>		
	<b>GAVI</b>	<b>Global Fund</b>	<b>GEF</b>
<i>Target of Fiduciary standards</i>	National entities	National or civil society entities (Principal Recipients)	MIEs using GEF funds
<i>Number of implementing entities per country</i>	One (assessed at country-level)	Multiple; previously one per programme; going forward will be two (one civil society and one national)	NA
<i>Nature of underlying services</i>	Mainly programmes	Mix of projects and programmes	Mix of projects and programmes
<i>Variety of services</i>	Low – two types of cash-based support including vaccine purchases for immunisation, and health systems	Low to medium – from procurement of goods and services for treatments through development of	High – complete range of projects including climate change related

	<b>Organisation</b>		
	<b>GAVI</b>	<b>Global Fund</b>	<b>GEF</b>
	strengthening	clinics	
<i>Accreditation and specific grant requests</i>	Accreditation (being phased in from 2009) will take place prior to new grant requests	Grant requests are made prior to accreditation	Self-accreditation requirement brought in from 2008
<i>Coverage of Fiduciary standards</i>	Solely financial	Financial, institutional	Financial, institutional, transparency/self regulation
<i>Role of financial standards</i>	Informational to assist capacity building and select funding mechanism	Pass/conditional pass/fail	Pass/fail
<i>Responsibility for assessment</i>	GAVI Secretariat (i.e. in-house)	External (Local Fund Agent)	Self assessment

These three entities provide good examples of different approaches to dealing with fiduciary risk, all of which have a degree of relevance to the AF.

### **3.2 GEF**

3.2.1 The approach of the GEF might be characterised as adopting the most wide-ranging application of the fiduciary standards of the organisations considered above. These standards, covering financial competencies, institutional/managerial capabilities and transparency/self regulation, have been developed specifically for the purpose of ensuring that MIEs meet the requisite standards to deal with the many different uses of GEF funds. Entities either meet or do not meet the standards, although we understand that each is responsible for self accreditation, with the fiduciary standards only being introduced latterly.

3.2.2 The GEF approach does not constitute direct access and the standards developed by the GEF may not be appropriate for direct access as they are developed specifically for multilaterals. However, some characteristics of the GEF approach are relevant and we have drawn on these in developing our proposals (e.g. whistleblowing).

### **3.3 GAVI**

- 3.3.1 At the other extreme, the GAVI adopts an approach based upon PEFA, focused on establishing the necessary safeguards to deal with the channelling of programmatic funds through national entities. The GAVI's Financial Management Assessment (FMA) system has been recently introduced to assess countries receiving cash-based funding, and is based on a 'slimmed down' version of the PEFA indicators, tailored to the health sector. However, rather than adopting a "pass/fail" approach, the FMA is aimed more at identifying areas of weakness which can be addressed through appropriate capacity building, and is used to select a mechanism for channelling funding, rather than to determine whether funding will be given.
- 3.3.2 The GAVI approach, in many ways, sets the use of local systems as almost as high an objective as the need to meet the standards themselves. To some extent the greater risks which might be associated with this approach are mitigated by the fact that GAVI typically funds multi-donor approaches with a wide range of partners and the fact that it supports a relatively limited "product" range - the funding of established programmes and the availability of many benchmarks across highly standardized approaches help limit the scope for fraudulent activities. In addition, the standardised approach means that the FMA can be specifically tailored to assessing the relevant capacities/systems within countries, notwithstanding that it does not relate to a specific grant proposal.
- 3.3.3 However, the non-financial fiduciary standards are assessed by other means, such as data quality audits carried out by the WHO, which means that GAVI's responsibility for ensuring appropriate fiduciary standards is limited to financial competencies. This means that the GAVI approach is relevant to financial fiduciary standards, but has less relevance to considerations of institutional technical capacity to implement projects.

### **3.4 Global Fund**

- 3.4.1 The GF approach is different from GAVI in a number of ways. Fiduciary standards, which cover institutional capabilities as well as financial integrity, must be met, although there is scope for accreditation requirements to be met with the support of third parties. The nature of the projects and programmes are more varied than GAVI, although perhaps not as much as is the case with GEF. However, GF accreditation takes place in the context of a specific grant application and therefore with full knowledge of what the grants are likely to be used for; as such, specific institutional capabilities can be assessed in the light of the challenges likely to be faced.
- 3.4.2 Whereas GAVI has sought to undertake accreditation assessment in-house and, in doing so, maximise its own institutional learning, the GF is heavily reliant on third party



assessors. Of all of the approaches to accreditation, the GF is perhaps seen as being most onerous by those being assessed. The issue of outsourcing versus “in house” accreditation is explored further in Section 7.2.

### **3.5 Applicability for Adaptation Fund**

3.5.1 We would argue, therefore, that different aspects of each of the above might be drawn on given the context of the AF. We consider that the range and technical complexity of the activities the AF is likely to encounter puts it in a context much closer to the GF and GEF (although the range of projects that the AF will fund is likely to be greater). Given the different “ownership” context in which the AF will be established, there are, however, aspects of the GAVI approach (and direct budgetary support to the extent that it uses information generated by PEFA) which may reflect this better.

3.5.2 In developing an approach to Fiduciary Standards for the AF, albeit one that is anchored in the approaches of similar programmes, we would emphasise that the following need to be built into any design:

- the fact that the recipients “own” the AF in a way they do not the other facilities, albeit within the UNFCCC framework;
- the need for the standards to cover an extremely wide range of projects and programmes, with differing NIE implementing competencies; and
- given the above, the need for fiduciary competences that go well beyond the pure financial, covering institutional capabilities and the need to address transparency requirements, ensure value for money in procurement, and include social and environmental safeguards.

3.5.3 In Section IV of this paper, we consider in more detail the specific fiduciary competencies that would be required from NIEs, illustrative methods of verifying these, and a means of addressing the issues posed by the differing NIE implementing competencies potentially required for AF projects/programmes.

## IV FIDUCIARY STANDARDS

In this section we set out in outline proposed fiduciary standards for the Adaptation Fund, by means of describing the competencies and specific capabilities required of NIEs, together with illustrative means by which these might be verified. At this point, these should be considered as illustrations rather than specific recommendations, as this is outside the scope of this paper.

### 4.1 Principles

4.1.1 It is important that the Board's approach to fiduciary standards is based on clear agreed principles.

4.1.2 In Decision CMP5/CMP.2 the Conference of the Parties decided that:

1. The Adaptation Fund shall be guided by the following principles:
  - a. access to the fund in a balanced and equitable manner for eligible countries;
  - b. transparency and openness in the governance of the fund;
  - c. accountability in management, operation and use of the funds;
  - d. efficiency and effectiveness in the management, operation and governance of the fund.
2. The Adaptation Fund shall operate with the following modalities:
  - a. competency in adaptation and financial management;
  - b. sound financial management, including the use of international fiduciary standards;
  - c. clearly defined responsibilities for quality assurance, management and implementation;
  - d. independent monitoring, evaluation and financial audits;
  - e. learning by doing.

4.1.2 In implementing fiduciary standards consistent with these general principles and modalities the Board should be guided by the following supplemental principles.

- a. to apply fiduciary standards that meet the Objectives outlined below; and
- b. to use existing country management systems and procedures to the extent that these are capable of achieving the Objectives outlined below;
- c. to transfer responsibility for implementation of projects and programmes to countries, and to monitor evaluate and review the performance of their implementation.

### 4.2 Purpose and Objectives

4.2.1 Overall **purpose** of the accreditation and grant application processes is to maximise direct access to AF funding by eligible Parties.

4.2.2 **Objectives** of the specific fiduciary standards are to:

1. ensure that allocated moneys are applied for the purpose for which they are intended; and
2. ensure that funds are spent in as efficient manner as possible in order to maximise value for money.

### 4.3 Required Competencies and Specific Capabilities

4.3.1 Table 4.3 below sets out the **required competencies** and **specific capabilities** required of NIEs to meet the standards. By way of explanation:

- *Required competencies* are the competencies that the NIE needs to demonstrate to meet the standards;
- *Specific capabilities* are the attributes which need to be demonstrated which underpin the required competency; and
- *Illustrative means of verification* are non-exhaustive examples of the forms of evidence which might demonstrate the specific capability.

*Table 4.3: Required Competencies and Specific Capabilities*

<b>Required competency</b>	<b>Specific capability required</b>	<b>Illustrative means of verification</b>
<b>I Financial integrity</b>	<i>The ability to accurately and regularly record transactions and balances to an appropriate standard as attested to by a competent entity</i>	<ul style="list-style-type: none"> <li>• Production of regular, reliable<sup>10</sup> financial statements</li> <li>• Audited/externally scrutinised accounts</li> <li>• Production of independently verified, detailed accounts</li> <li>• Installation of internationally recognised accounting packages (eg SAGE)</li> </ul>
	<i>The ability to safeguard, manage and disburse funds efficiently to</i>	<ul style="list-style-type: none"> <li>• Financial projections demonstrating financial solvency</li> <li>• Demonstration of proven payment systems</li> </ul>

<sup>10</sup> i.e. materially correct.

Required competency	Specific capability required	Illustrative means of verification
	<i>recipients on a timely basis</i>	
	<i>The competency to produce forward-looking financial plans and budgets</i>	<ul style="list-style-type: none"> <li>• Evidence of preparation of corporate or departmental / ministry budgets</li> <li>• Detailed analyses of previous outturns versus budgets</li> </ul>
	<i>Legal status to contract with AF and third parties</i>	<ul style="list-style-type: none"> <li>• Demonstration of necessary legal personality</li> </ul>
<b>II Requisite institutional capacity</b>	<i>Procurement procedures which provide for transparent competition including effective means of redress</i>	<ul style="list-style-type: none"> <li>• Evidence of procurement policies and procedures consistent with best practice (ie transparency, competitive tendering)</li> </ul>
	<i>Capacity to undertake monitoring and evaluation</i>	<ul style="list-style-type: none"> <li>• Availability of resources to implement agreed monitoring and evaluation framework, including: <ul style="list-style-type: none"> <li>(i) preparation of regular reliable programmatic reports</li> <li>(ii) demonstration of ability to undertake systematic collection of relevant data for the purposes of evaluations and other studies.</li> </ul> </li> </ul>
	<i>Ability to identify, develop and appraise project – ex ante and ex post – technically, legally, financially, economically,</i>	<ul style="list-style-type: none"> <li>• Availability of resources to conduct requisite ex-ante and ex-post appraisals of projects of a similar complexity</li> </ul>

Required competency	Specific capability required	Illustrative means of verification
	<i>socially and environmentally (as appropriate)</i>	
	<i>Competency to manage or oversee the execution of the project including ability to manage sub-recipients, fit for purpose infrastructure and resource to support project delivery and implementation</i>	<ul style="list-style-type: none"> <li>• Comprehensive understanding of and capacity to address the technical, financial, economic, social, environmental and legal aspects of the project and their implications</li> <li>• Demonstrated competence to execute or oversee execution of projects or programmes of the same nature as the intended project or programme.</li> </ul>
<b>III Transparency and self - investigative powers</b>	<i>Freedom to whistle-blow on issues of fraud and gross mismanagement</i>	<ul style="list-style-type: none"> <li>• Demonstration of a written policy and / “fraud hot-line”</li> <li>• Whistle-blower protection policies<sup>11</sup></li> </ul>
	<i>Objective policy for self-regulation</i>	<ul style="list-style-type: none"> <li>• Policies for maintaining accreditation and for addressing any problems as they arise</li> </ul>

#### 4.4 Minimum requirement for Conditional Accreditation

4.4.1 Note that the capabilities required under III (Transparency and Self-Investigative Powers) above are not capable of being outsourced or provided externally to an NIE.

#### 4.5 Accreditation stage and project proposal stage

4.5.1 As set out in the previous section, we would argue that the competencies and capabilities set out in II (Requisite Institutional Capacity) can only be assessed in the context of an

<sup>11</sup> Avenues for reporting suspected ethics violations and protections for individuals reporting such violations.

individual project or programme proposal. This is because the competencies and capabilities for the project proposal stage will vary widely depending on the nature of the project. This means that these competencies and capabilities cannot be assessed in an absolute sense, they need to be considered relative to the implementation capability demands of the specific proposed project or programme, as these will vary tremendously.

- 4.5.2 For NIE's that already have a track record in implementing projects and programmes the assessment will take into account the entities track record (e.g. successful implementation of similar projects and programmes). Where the entity is new or does not have a track record the resources available to the entity to fulfil these capacity requirements will be assessed.
- 4.5.2 In consequence, any project proposal would need to demonstrate how the fiduciary standards set out in II (Requisite Institutional Capacity) would be achieved in the context of a given project. As with financial accreditation, the NIE could choose to demonstrate these capabilities in different ways, with the support of third parties or with the assistance of an MIE.
- 4.5.3 The assessment of institutional capabilities (ie standards set out in II (Requisite Institutional Capacity)) will be led by the Secretariat (possibly with specialist technical external support) in order to build up institutional learning of the capabilities of the different NIEs. This contrasts with financial accreditation where there will be a greater reliance on third parties.

#### **4.6 Future proposals**

- 4.6.1 Once an NIE has successfully undertaken a project or programme of a given type, which demonstrates the requisite institutional capabilities, it would (if successful) be considered competent to undertake similar programmes, or less complex programmes, in future. In assessing future proposals, the AF would of course need to satisfy itself that the capabilities demonstrated previously were relevant to the new proposal.

#### **4.6.2 *Process for project fast-track***

The NIE, when submitting its project proposal, will be required to specify whether it believes that the proposal qualifies for fast-tracking, giving reasons, e.g. the technical simplicity of the project or the fact that the NIE has undertaken a project of this kind successfully before. The Board will review requests and decide whether an application qualifies for fast track.

## V FINANCIAL ACCREDITATION

### 5.1 Overview

- 5.1.1 In this section we outline the proposed process for the financial accreditation of the NIEs and the approval of proposals by the Board. The proposed process, if approved, can form the basis for the section of the draft Policies and Procedures under the heading “Accreditation of Implementing Entities”.
- 5.1.2 We propose that there should be two “gateways” to “direct access” via the accreditation process for NIEs, as outlined in the remainder of this section: “Accreditation” and “Conditional Accreditation”. If neither Accreditation nor Conditional Accreditation can be achieved by a prospective NIE, the eligible Party would be required to access AF funding via an MIE, until it is able to put forward an NIE able to obtain Accreditation or Conditional Accreditation.
- 5.1.3 However, we would argue that they should cover dimensions of financial integrity, institutional capacity to undertake projects and the ability to self-regulate and whistle blow. As we will explain in detail in the next section, however, it is not possible to assess institutional capacity (i.e., those capabilities set out under the heading II (Requisite Institutional Capacity)), except in relation to a specific project or programme. Therefore *ex ante* accreditation (that is, ahead of a specific proposal or application) can only be applied to the other standards (i.e., those capabilities set out under the headings I (Financial Integrity) and III (Transparency and Self-Investigative Powers)), which are largely financial in nature. Thus, we have limited *ex ante* accreditation to those capabilities set out under the headings I (Financial Integrity) and III (Transparency and Self-Investigative Powers).

### 5.2 Accreditation of MIEs

- 5.2.1 We note that in paragraph 33 of the draft Policies and Procedures the Board will invite potential MIEs to express interest in serving the AF. In order to harmonise with existing systems and avoid unnecessary duplication, we assume that the MIEs which have already reported on their compliance with the GEF’s fiduciary standards will be automatically accredited for the purposes of the AF.

### 5.3 Accreditation and Project/Programme Approval

- 5.3.1 Although it should be possible to achieve an accreditation prior to making an application for a grant or other monies, NIEs should be encouraged to seek accreditation in parallel to applying for a grant (in order to avoid unnecessary work and to give a focus to the accreditation).

5.3.2 In addition, there are certain institutional competencies required of an NIE (i.e. , those set out under the heading II (Requisite Institutional Capacity)) that will vary so widely according to the specific project/programme that they cannot be included in a generic advance ‘accreditation’ but will need to be considered separately as part of the project approval process. For example, the technical capabilities of an organisation and its individual personnel required to carry out procurement and monitoring and evaluation, will vary widely depending upon the technical requirements of the specific project/programme. These will therefore be considered as part of the project approval process rather than the accreditation process. The accreditation process and the project approval process are therefore closely linked.

#### **5.4 Submission of applications**

5.4.1 Eligible Parties will submit applications for accreditation of NIEs directly to the Board.

5.4.2 The proposal will include a detailed **self-assessment** of how the NIE’s own systems meet the financial and some other fiduciary standards described in Section V with appropriate relevant supporting documentation describing the NIE’s financial and project and programme management systems including:

- national rules and regulations;
- policies and procedures; and
- external assessments of these e.g. Public Expenditure and Financial Accountability (PEFA) reports, World Bank Country Financial Accountability Assessment (CFAA) reports, bilateral donor fiduciary risk assessments e.g. for direct budgetary support, etc.

5.4.3 This ‘self-assessment’ element of the process is intended to give eligible Parties a greater understanding of and involvement in the fiduciary risk management process and to avoid the accreditation process being perceived as a ‘pass/fail’ exercise being imposed by the Board. Rather, the Parties themselves are encouraged to demonstrate how they will meet the required standards (with MIE/bilateral/third party assistance if required), which should allow them to identify and remedy any potential issues in advance.

#### **5.5 Assessment**

5.5.1 On receipt of the proposal the Board, through the Secretariat, notifies the Assessment Review Panel (ARP) of the application, commissions a reputable advisory firm (the Assessor) to assess whether the NIE meets the fiduciary standards and assigns a member of the Secretariat to the assessment process. The report will highlight for the Board any areas where the NIE does not meet the fiduciary standards.

5.5.2 The role and composition of the ARP, and the reasoning for outsourcing the assessment role, are discussed in more detail in Section VII.



5.5.3 The assessment team (comprising the Assessor working with the member of the Secretariat) undertakes the assessment in two stages:

- (i) a desk review, considering the documents submitted by the NIE with its proposal, together with any other relevant existing public financial and fiduciary management assessments; and
- (ii) an in-country review (which will vary in depth/scope depending on the availability and reliability of information reviewed under the desk review), consisting of interviews with relevant individuals within the NIE to verify or build on the information already obtained.

5.5.4 The Assessor then prepares a report on the NIE's compliance with the AF's fiduciary standards, highlighting any areas of non-compliance, and submits the report to the ARP through the Secretariat.

## 5.6 Financial accreditation

5.6.1 The ARP undertakes a detailed technical review of the application and makes a recommendation to the Board. The review will assess the application against the fiduciary management standards set out in Section IV.

5.6.2 The ARP may recommend to the Board:

- (i) that the NIE meets the fiduciary standards and should be accredited ("**Accreditation**");
- (ii) that the NIE does not meet the fiduciary standards in all respects but may be reconsidered for accreditation if it addresses areas where it does not meet the fiduciary standards, through, for instance, relying on verifiable third party capabilities in its areas of weaknesses ("**Conditional Accreditation**"); or
- (iii) that the NIE does not meet the fiduciary standards required, and is unlikely to do so even with third party assistance. In this case, the eligible Party would be required to access AF funding indirectly via an MIE, until it were able to put forward (either the same or a different) NIE able to obtain Accreditation or Conditional Accreditation ("**MIE Support**").

### 5.6.3 *Accreditation*

If, having considered the recommendation of the ARP, the Board determines that the NIE should be accredited, the Board requests the Secretariat to confirm to the NIE that it is accredited to implement projects funded by the AF (subject to those capabilities required to be demonstrated at the project proposal stage (as discussed in Section IV I (Financial

Integrity) and III (Transparency and Self-Investigative Powers)), and follows up with the NIE on applications for AF funding.

#### 5.6.4 *Conditional Accreditation*

A conditional accreditation may be achieved, either by the NIE applying for such a status, after its own self appraisal suggests this to be the most appropriate route, or if it fails a full accreditation assessment. In this latter scenario, if the Board determines Conditional Accreditation the Board will request the Secretariat to confirm that the NIE has not met the financial and other fiduciary standards, and to consult with the NIE as to how third party support (including from an MIE or bilateral donor) might be utilised to address those areas where it has not met the fiduciary standards (for instance, to manage finances or aspects of project preparation).

These discussions will need to cover both how the required fiduciary standard can be met in the short term (for example, through contracting in external financial management support), and how capacity might be built in the longer term through technical assistance support, with a view to allowing the NIE to meet the standard itself and to submit for full accreditation in due course.

In each case (short term support and long term capacity building), the question of funding will need to be considered. One possibility (if funds are available within the AF) is for the AF to hold discussions with potential providers of third party support and establish an agreed list of providers, and a process/parameters for funding both short term technical support and longer term capacity building. The eligible Party/NIE itself is then responsible for negotiating any arrangements with the relevant provider of third party support, although the AF may provide the required funding, providing the arrangement and provider fall within the agreed parameters. This would allow the countries to maintain responsibility for the process and to chose to work with existing partners (and therefore coordinate with existing capacity building programmes) where possible, whilst allowing the AF to ensure that funding allocated to capacity building is properly applied.

#### 5.6.5 *MIE Support*

As with Conditional Accreditation, the NIE can opt for this approach initially. It will also be the modus operandi if the Board determines that the NIE does not meet the fiduciary standards and should access AF funding for the meantime via an MIE. In such an instance, the Board requests the Secretariat to consult with the NIE to procure assistance from an MIE and to address the areas where it does not meet the fiduciary standards with a view to re-submitting an application for accreditation at a later date.

The considerations set out under ‘Conditional Accreditation’ above with respect to the responsibility for the commissioning and funding of technical assistance and capacity building apply equally to any assistance required by an NIE under this section.

An NIE may appeal against a decision of the Board in accordance with the AF appeal process.

## **5.7 Timing**

- 5.7.1 The AF would be required to complete the accreditation process within 6 - 12 months of the submission of an application that complies with the AF’s published application requirements. It should be noted that from our understanding Global Fund accreditations can take up to 18 months.

## **5.8 Fast Track at the Project Proposal Stage**

- 5.8.1 All NIEs will be required to demonstrate that they meet the capabilities set out under sections I (Financial Integrity) and III (Transparency and Self - Investigative Powers) described in Table 4.3. They will also be required to meet the capabilities set out under section II (Requisite institutional capacity) as described in Table 4.3 as part of the project proposal process before receiving AF funding.

- 5.8.2 However, if an NIE has been accredited as meeting the capabilities set out under sections I (Financial Integrity) and III (Transparency and Self - Investigative Powers), projects put forward by that NIE which meet certain criteria may qualify to be ‘fast-tracked’ at the project proposal stage. By fast-tracking we mean that there is a less exhaustive assessment of institutional capabilities at the proposal stage, which should have the impact of speeding up the approvals process.

### *5.8.3 Criteria for fast-track*

Initially, fast-tracking is likely to apply to projects which are:

- (i) Small-size Projects and Programmes (being those requesting up to US\$1 million, as defined by the Policies and Procedures); and
- (ii) Technically simple (for example, a simple procurement of goods or services); in other words, where the NIE is relying on a relatively limited range of institutional capabilities.

In future years, fast tracking may also be extended to cover projects/programmes where:

- the NIE has been accredited for and successfully carried out a similar project/programme; or
- the project is an extension of existing project/programme.

## VI PERFORMANCE MANAGEMENT

We have set out brief outline of an approach to performance management of accredited NIEs below.

### 6.1 Maintaining Accreditation

- 6.1.1 Accreditation, incorporating all three groups of capabilities, is not a one-off, but an ongoing process.
- 6.1.2 The Secretariat will work closely with the NIEs to support them in ensuring that they continue to meet the fiduciary standards.
- 6.1.3 Under the draft Policies and Procedures the NIE's are required to submit annual status reports on their projects and programmes.
- 6.1.4 NIEs will also include within their annual reports a periodic self-assessment of their fiduciary management systems. The report will update the Board on the performance of the NIE's own systems against the AF fiduciary standards set out in Section IV.
- 6.1.5 The Board through the Secretariat will undertake or commission from an Assessor a periodic (eg every 2 years) assessment report of the NIE's performance against the fiduciary standards. The Board may also commission ad hoc special investigations where these are necessary.
- 6.1.6 The Assessor submits the report to the Board through the Secretariat highlighting areas where the NIE no longer meets the fiduciary standards for which it has previously been accredited. The Assessor will review the NIE's self-assessment and follow up with an in-country review, consisting of interviews with relevant individuals within the NIE to verify or build on the information already obtained.
- 6.1.7 The Board may request that the ARP review the report and make a recommendation either (i) that the NIE should continue to be accredited or (ii) that there are areas where the NIE fails to meet the fiduciary standards. The Board makes a determination.
- 6.1.8 If the Board determines that the NIE no longer meets the fiduciary standards the Board will request the Secretariat to confirm to the NIE that it is no longer accredited, and may re-submit for accreditation when it addresses the areas where it does not meet the fiduciary standards. The AF Secretariat will consult with the NIE on how to address the areas where it does not meet the fiduciary standards, and on procuring assistance from an MIE or other service provider to address the areas where it does not meet the fiduciary standards with the a view to submitting an application for re-accreditation at a later date, and to supporting the on-going implementation of the AF funded projects that the NIE is currently implementing.

6.1.9 The considerations set out in paragraph 5.6.4 above, under ‘Conditional Accreditation’, with respect to the responsibility for commissioning and funding of technical assistance and capacity building apply equally to any assistance required by an NIE under this section.

## **6.2 Risk management/early warning**

6.2.1 It is proposed that the Board should consider developing a risk management/early warning system to assist the Board in identifying projects/programmes that potentially give rise to a significant risk for example because of value, complexity and other factors. The operation of an effective risk management system should assist the Board in reducing the bureaucracy involved in monitoring the grant funding.

## **6.3 Misuse of funds - consequences**

6.3.1 The draft Policies and Procedures make provision for the cancellation, termination and suspension of projects where financial irregularities are found. The Board may also consider terminating the accreditation of an NIE in such circumstances.

## VII IMPLEMENTATION ISSUES

### 7.1 Governance

#### 7.1.1 *Board Role and Responsibilities*

The Board has fiduciary responsibility for the proper application of the AF's funds.

The Board will be responsible for all decisions to accredit NIEs, and all project and programme approvals and performance monitoring.

#### 7.1.2 *Committees of the Board*

It is understood that two committees of the Board have been constituted<sup>12</sup>:

- (i) **The Ethics and Finance Committee (EFC)**, responsible for providing advice to the Board on issues of conflict of interest, ethics, finance and audit.
- (ii) **The Project and Programme Review Committee (PPRC)**, responsible for assisting tasks of the Board related to project/programme reviews included in the AF's project cycle, for monitoring the functions of the core governance structures of the AF, and for providing advice on them to the Board on the basis of the Results-Based-Management framework of the AF's portfolio, and providing advice to the Board on all strategy and policy issues related to the AF's portfolio.

7.1.3 The accreditation review process will require technical and financial expertise in a range of areas.

7.1.4 The Board could obtain assistance from the PPRC in the accreditation review process by widening its terms of reference. The alternative, and in our view a significantly more appropriate option, would be for the Board to seek such support from an independent panel. Our proposal for the independent panel is described below.

#### 7.1.5 *Accreditation Review Panel*

The Board would establish an independent Accreditation Review Panel (ARP). The ARP would be made up of independent technical experts. The ARP would report to the Board.

The ARP members could either be paid by the AF or could undertake the work on a pro bono basis. It is recommended that if possible the work should be undertaken on a pro bono basis.

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<sup>12</sup> Board Decision B.5/5.

The TOR for the ARP could include advising the Board in the accreditation and review process, performance management, and accreditation appeal process.

#### 7.1.6 *Relative advantages of use of ARP and PPRC to support accreditation*

The relative advantages and disadvantages of the options are set out below.

	<b>PPRC</b>	<b>ARP</b>
<b>Advantages</b>	<ul style="list-style-type: none"> <li>Aligns activity with project/programme approval</li> <li>Direct control of the Board through participation of Board members</li> </ul>	<ul style="list-style-type: none"> <li>Independent technical judgement brought to bear</li> <li>Frees up time for Board members</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>Lacks independence</li> <li>Absorbs Board member time</li> </ul>	<ul style="list-style-type: none"> <li>Not under full direct control of Board with independent participants</li> </ul>

7.1.7 The Board is responsible for the performance management of all entities receiving AF funds or providing services to the AF.

7.1.8 The EFC is responsible for the AF's audit function. This responsibility should cover the audit of NIE recipients in case of alleged fraud or misuse of funds.

7.1.9 The PPRC provides advice to the Board on a variety of matters relating to the project and programme approval and review process, and in the project appeal processes.

#### 7.1.10 *Secretariat Role and Responsibilities*

The Secretariat will support the Board in the accreditation review process, and exercise any powers specifically delegated to it by the Board. This may involve the engagement of external service providers as Assessors, as discussed in Section 7.2 below.

## **7.2 Institutional Implications**

7.2.1 The accreditation review and performance monitoring process will require the dedication of considerable resources to ensure that the Board is able to fulfill its fiduciary commitments in respect of the AF's funds. A detailed assessment of these resources is outside the scope of our work.

7.2.2 We have proposed that the Board should engage external service providers as Assessors to support the financial accreditation, and performance monitoring processes. The relative advantages and disadvantages of outsourcing these functions are set out below:

	<b>In-house</b>	<b>Outsourced</b>
<b>Advantages</b>	<ul style="list-style-type: none"> <li>• Knowledge kept in-house</li> <li>• Probably cheaper</li> </ul>	<ul style="list-style-type: none"> <li>• Independent specialist professional judgement brought to bear</li> <li>• Professional reputation and PI insurance of service provider provides assurance to the Board</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>• Insufficient distance between review team and NIE</li> <li>• Increased bureaucracy in the AF</li> </ul>	<ul style="list-style-type: none"> <li>• Knowledge potentially lost on change of service provider</li> <li>• Cost</li> </ul>

7.2.3 The external service providers will be engaged through an international competitive process, and would be required to re-tender for the provision of services to the AF on a periodic basis as good practice. This means that the understanding developed by the service providers of the NIEs’ capability would be lost. This could be mitigated by a member of the Secretariat being “embedded” in the accreditation review team so that the AF itself develops an understanding of the capacity of the NIEs. As set out, assessment of institutional capabilities should be led by the Secretariat to maintain learning and knowledge “in-house” as this is the most difficult area to assess, and is subject potentially to most development/change.

7.2.4 The Assessors will need to have the requisite capability in the assessment of the competencies and capabilities of the NIEs only in the financial and associated areas which are required to meet the fiduciary standards.

7.2.5 It will be important in designing the incentive arrangements of the Assessors to ensure that these are fully aligned with the AF’s principles, purpose and objectives as outlined in Section IV. It is understood that recent changes in the Global Fund remuneration arrangements potentially discourage initiative from their service providers.

7.2.6 As noted above, we consider that the assessment of the requisite institutional capacity (i.e. standards as set out in II (Requisite Institutional Capacity) in Section IV) required for the project proposal stage and, as regards individual projects, the competencies and capabilities to undertake procurement and monitoring and evaluation in relation to the specific project, will require specialist expertise relevant to the individual projects in



question. The secretariat may hire additional support from different sources for the institutional capabilities assessment.

- 7.2.7 In total, the procurement of the professional services required to support the Board in the project and programme proposal assessment process will need to need to cover potentially a very wide range of expertise.

### **7.3 Financial implications**

- 7.3.1 A detailed assessment of the work involved and therefore the cost of each accreditation and performance management review is outside the scope this report. However, our initial estimate is that each financial accreditation review, if undertaken by a third party service provider would take between 15 to 30 person days, and cost between USD 30,000 to 60,000, depending of course on the complexity of the entity being reviewed.

- 7.3.2 Our initial estimate of the cost of each NIE performance management reviews is that it would take between 10 and 20 person days and cost between USD 20,000 and 40,000 depending on the complexity of the entity being reviewed.

### **7.4 Stepwise implementation**

- 7.4.1 The terms of reference ask for a review of the potential for step-wise implementation. We would argue that the proposed approach already provides for this, in terms of a proven capability increasing the speed at which future projects falling within this capability might be assessed. As an option, treating procurement as a financial rather than institutional standard for the purposes of basic procurement may assist this approach further by allowing NIEs to undertake procurement for less complex projects on the basis of the initial accreditation.

- 7.4.2 It is clear that financial accreditation has to be in place before any monies can be disbursed to the NIE, although this might be undertaken in parallel to a specific project/program proposal. Therefore, whatever, their final content, the standards in I (Financial Integrity) and III (Transparency and Self-Investigative Powers) in Section IV must be met as a matter of urgency. Moreover, of the standards, these are perhaps the most discrete, in the sense that they are absolutes – a given NIE either meets them or does not, irrespective of the given scale or complexity of a given project/program – except in the extreme.

- 7.4.3 The institutional capabilities are, however, more varied, not just relative to the other types of standard but also between themselves. Whereas the abilities to develop projects and to manage them will show a considerable variance in terms of capability, the procurement standard is slightly more absolute, along the lines of the financial standards.

7.4.4 Given this, there may be an argument for grouping procurement with the financial standards. The effect of this would be to enable the fast-tracking of many more straight-forward projects of a size greater than the USD 1 million threshold.

## 7.5 Compatibility with Paris Principles

7.5.1 It is noted that the proposals in this paper are required to be aligned, to the extent deemed possible and relevant, with the key principles of the Paris Declaration on Aid Effectiveness.

7.5.2 Table 7.5 below summarises the Paris principles and key indicators, and how these are addressed by the proposals set out in this paper and the AF's existing systems.

Table 7.5: Paris Principles

<i>Principle</i>	<i>Alignment</i>
<i>Country ownership</i>	Proposals are originated within country by NIE put forward by country
<i>Alignment</i>	
<i>Use of country procurement and public financial management systems</i>	Proposed accreditation system allows NIEs to use their own procurement and PFM systems to the extent that these meet the minimum fiduciary standards
<i>Aid flows aligned on national priorities</i>	Proposals are originated within country by NIE put forward by country
<i>Strengthen capacity by coordinated support</i>	To the extent that NIE is not fully accredited, proposed system allows for conditional accreditation and short term support/long term capacity building. Allowing countries to propose their own arrangements for capacity building (within AF parameters) will allow for coordination with existing bilateral/multilateral capacity building initiatives
<i>Strengthen capacity by avoiding parallel implementation</i>	Depends on identity of NIE: countries are free to nominate an existing ministry or

<b><i>Principle</i></b>	<b><i>Alignment</i></b>
<p><i>Aid is more predictable</i></p> <p><i>Aid is untied</i></p>	<p>agency where a suitable entity is available</p> <p>Pre-accreditation should allow issues to be addressed up front and therefore funding to be disbursed regularly once NIE and proposal is approved</p> <p>N/A</p>
<p><b><i>Harmonisation</i></b></p> <p><i>Use of common arrangements or procedures</i></p> <p><i>Encourage shared analysis</i></p>	<p>Where NIEs are not independently accredited, assistance in implementation is likely to be given by existing bilateral/multilateral partners</p> <p>Proposed ‘desk review’ stage of accreditation process relies on available existing analysis</p>
<p><b><i>Results based frameworks</i></b></p>	<p>NIEs’ M&amp;E and project appraisal capacity is assessed in relation to each project at the project proposal stage to ensure capability</p>
<p><b><i>Mutual accountability</i></b></p>	<p>Governance arrangements within AF provide for balanced representation of countries on the Board</p>

## Appendix 1

### GAVI and Global Fund Approach to Fiduciary Standards and Devolved Management

#### GLOBAL FUND

Under the Global Fund system, prior to a project grant being approved, the financial management and administrative capacity of the Principal Recipient (PR) must be verified. The PR is the public or private organisation nominated by the country's Country Coordinating Mechanism (CCM) to be the principal grant recipient and undertake certain implementation functions in relation to the grant. (Note: under the Global Fund's new 'dual track financing' requirements, two PRs must be nominated by each CCM: one from government and one from civil society.)

This verification process has similar aspects to the proposed National Implementing Agency accreditation process for the Adaptation Fund. However, in the case of the Global Fund the verification takes place only after the CCM has submitted a grant proposal which has been reviewed and approved by the Board and (from a technical perspective) by the Technical Review Panel. Therefore the verification relates only to the PR's capacity to implement the specific proposal and is not a more general accreditation to implement other projects.

*Who carries out the verification?*

The verification is carried out by the Local Fund Agent (LFA) for that country. The LFA is an external consultancy selected by the Global Fund for each country under a competitive tender process for a period of four years.

*What are the minimum criteria?*

Under the initial verification, the PR(s) must demonstrate financial management and administrative capacity meeting the following minimum criteria (preferably within existing systems):

- (a) Financial Management and Systems that:**
  - (i) Can correctly record all transactions and balances, including those supported by the Global Fund;
  - (ii) Can disburse funds to sub-recipients and suppliers in a timely, transparent and accountable manner;
  - (iii) Can support the preparation of regular reliable financial statements;
  - (iv) Can safeguard the PR's assets; and

- (v) Are subject to acceptable auditing arrangements.
- (b) Institutional and Programmatic arrangements that include:**
  - (i) Legal status to enter into the grant agreement with the Global Fund;
  - (ii) Effective organizational leadership, management, transparent decision making and accountability systems;
  - (iii) Adequate infrastructure and information systems to support proposal implementation, including the monitoring of performance of sub-recipients and outsourced entities in a timely and accountable manner; and
  - (iv) Adequate health expertise (HIV/AIDS, tuberculosis and/or malaria) and cross-functional expertise (finance, procurement, legal, M&E).
- (c) Sub-recipient Management capacity, including:**
  - (i) Effective systems for undertaking sub-recipient capacity assessments and providing technical support as needed, to ensure that any proposed sub-recipients have the required capacities to implement the program activities; and
  - (ii) Adequate management arrangements that ensure adequate PR oversight of grant implementation at the sub-recipient level facilitating effective and timely program implementation and resource management by sub-recipients.
- (d) Procurement and Supply Management Systems that can:**
  - (i) Provide a basic procurement supply and management plan which outlines how the PR will adhere to the Global Fund's procurement principles;
  - (ii) Deliver to the end-user adequate quantities of quality products in a timely fashion (especially in the area of health products) that have been procured through a transparent and competitive process; and
  - (iii) Provide adequate accountability for all procurement conducted.
- (e) Monitoring and Evaluation arrangements that can:**
  - (i) Collect and record programmatic data with appropriate quality control measures;
  - (ii) Support the preparation of regular reliable programmatic reports; and
  - (iii) Make data available for the purpose of evaluations and other studies.

Guidelines, forms, checklists and questionnaires are available for the evaluation.

*What is the result of the verification?*

LFA will determine that the PR:

- (a) has the required minimum capacities and systems;
- (b) needs to acquire certain additional capacities and is able to do so in a timely and cost effective manner, or
- (c) requires major capacity strengthening that appears excessive under the circumstances.

The assessment report will be discussed with the PR, who should identify ways to supplement its capacities or otherwise address any identified weaknesses.

Based on the assessment, the Global Fund will decide whether to enter into a Grant Agreement with a nominated PR and which capacity-strengthening measures or other actions that PR must achieve before the first or a subsequent disbursement of funds. Such measures or actions will be included as conditions precedent in the Grant Agreement. The PR, assisted by other members of the CCM as appropriate, decides how the necessary capacity strengthening may be acquired and which entities may be of assistance for this purpose. Development partners may provide or participate in such capacity building activities.

In case (c) above, the Global Fund may ask the CCM to identify one or a few suitable alternative PR(s). In exceptional cases, should no local stakeholder be qualified to be PR, the Global Fund may agree to the local office of a multilateral organization assuming PR responsibilities. Such arrangement should be temporary and local entity(ies) should be phased-in as PR(s) once capacity is strengthened.

An Internal Appeal Mechanism allows applicants whose proposals were rejected in two consecutive rounds to appeal the second decision.

### **Ongoing requirements**

The initial verification is only part of the Global Fund fiduciary risk management system. Other aspects include:

*Continuing assessment by the LFA*

- Six months into the programme, the LFA is required to review and report on the PR's progress as a condition to receipt of the second tranche of funding.

- Two years into the programme, a major ‘Phase 2’ assessment is carried out by the LFA, and a new recommendation made on a similar basis as to whether to continue with funding and enter into a new grant agreement for the next three years.

### *Annual reporting*

LFAs are responsible for verifying the performance of grant-funded programs each time recipients report results.

The PR submits fiscal year progress report and annual audit of program financial statements to the LFA. Audit requirements of the Global Fund are based on donor harmonization and OECD/DAC best practice recommendations. Applicable international audit standards or national standards consistent with international standards should be used. The LFA reviews the audit report, and advises the Global Fund on the appropriate response to any issues identified therein. The LFA does not itself audit the program financial statements.

### *M&E*

The PR is primarily responsible for monitoring and evaluation and submits periodic disbursement requests with updates on programmatic and financial progress. The LFA will review these.

The LFA is also responsible for ad hoc assignments undertaken at the request of the Global Fund, such as investigations relating to the suspected misuse of funds.

## GAVI

### **Financial Management Assessments**

Under its Transparency and Accountability Policy (TAP), adopted in June 2008, GAVI introduced a system of financial management assessments (FMAs) for countries receiving cash-based support, which took effect from 1 January 2009. FMAs have some similarities to the proposed accreditation system for NIEs, although FMAs focus on financial management capacity only (with particular emphasis on the health sector) and not other implementing functions (for example, those relating to technical capabilities; the GAVI covers these aspects in other ways, such as the use of data quality audits carried out under WHO procedures).

#### *Who carries out the FMA?*

Various options were considered by GAVI as to who might carry out FMAs. UNICEF, WHO and the World Bank indicated that they would not take on responsibility for this (although were willing to share materials and resources).

Fully outsourcing FMAs to external consultants was considered. However, it was decided that complete reliance on consultants would not only prove costly but it would not allow GAVI to build the knowledge base necessary for a consistent and responsive approach. The World Bank also raised this as an issue and concurs that GAVI should build internal capacity.

It was therefore decided that the Secretariat should recruit and hire four staff with expertise in country public financial management. It is envisaged that this will allow FMAs to be phased in within two years in all eligible countries, at a cost of approximately US\$ 6 million over two years. The Secretariat will still make use of external consultants as required, particularly for in-country assessments.

#### *What is the purpose of the FMA?*

The FMA is not a 'pass/fail' exercise. It is intended to provide a baseline understanding of the level of fiduciary risk in each country; help each country identify the most appropriate modality for channelling GAVI cash funds that provides adequate fiduciary assurance and indicate what additional criteria and steps may be needed in each country to mitigate potential risks.

Following the completion of the FMA, each country will be placed in one of three groups:

“Group I countries”: GAVI eligible countries that will channel and manage their GAVI cash transfers through existing joint financing mechanisms. Group I countries are assumed to represent the lowest level of fiduciary risk as they will have established procedures for financial management, procurement and reporting, with consistent oversight and support from in country development partners.



“Group II countries”: These countries follow varying procedures when managing donor funds. Group II countries will pose varying levels of fiduciary risks. Together with countries and in-country partners, the Secretariat will determine the most appropriate financing mechanism.

“Group III countries”: GAVI eligible countries in which there has been suspected or verified misuse of funds from GAVI cash transfers. The decision to include any single country in this category is subject to the judgment and discretion of GAVI management. Special procedures will be negotiated on a case-by-case basis.

In contrast with more rigid approaches like the Global Fund’s Local Fund Agent (LFA) system, GAVI is optimistic that this system will support country ownership and build upon individual countries’ systems and preferences.

*What are the minimum standards?*

The TAP is based on the requirement that GAVI cash funding should meet the following minimum standards:

- a) Funding should be used for purposes stated within a proposal;
- b) Funds must be managed in a transparent manner, and provide accurate and verifiable financial reports on a regular basis as specified by individual funding arrangements;
- c) Funds must be managed within accounts that meet national legal requirements for auditing, accounting and procurement.

*What does the FMA cover?*

The key areas will follow the PEFA framework and each area will receive a risk ranking as for CFAAs and PEFA evaluations.

Key areas for assessment include:

- i. National planning processes;
- ii. National budget development and execution process;
- iii. Legislative and regulatory framework for financial management;
- iv. The system for public sector accounting and internal control mechanisms;
- v. Financial recording systems;
- vi. National procurement processes;

- vii. National auditing and oversight capacity.

*How is the FMA carried out?*

The FMA is carried out by the Secretariat, working jointly with countries and bringing in external resources where required. It will consist of two stages:

- (a) The “macro assessment”/desk review: a review of findings from existing public financial and fiduciary management assessments and other diagnostic work, on both national and health sector public financial management practices, including, but not limited to:
- National rules and regulations for public financial management;
  - Public Expenditure and Financial Accountability (PEFA) reports;
  - World Bank Country Financial Accountability Assessment (CFAA) reports;
  - Documentation on joint financing arrangements for development partners in the health sector;
  - UNDG Harmonised Approach to Cash Transfers (HACT) reports;
  - Any additional reports (existing fiduciary risk assessments) that assess public financial management and procurement systems.
- (b) The “micro assessment”/in-country review: conducted primarily through interviews with Ministry of Finance and Ministry of Health staff and major development partners. It will allow GAVI to discuss and verify findings from the macro assessment with the government, and will narrow the focus of any further analysis to practices within the health sector, with specific emphasis on the mechanism selected to manage GAVI funding. In-country reviews may vary in scope and intensity depending on: the information obtained during the desk review; whether other partners are undertaking or have recently completed similar assessments; and the type of financing mechanism proposed by the country. In some cases, it may be considered that this stage is not necessary. Where high intensity in country reviews are required, external consultants are more likely to be involved.

*Frequency*

FMA will be repeated every 3 years.

## **Other features of the TAP**

The FMA is only one aspect of the TAP. Other key features to address risk on an ongoing basis include updated annual reporting and audit requirements for the countries, the implementation of an ‘early warning system’ and measures to be taken for suspected misuse of funds.

### *Reporting and audit*

Annual audit reports on the use of GAVI funds must be submitted by each country’s relevant national authority with the annual progress report, certified by the national auditing authority or an external audit firm.

The Independent Review Committee (IRC) team will then evaluate the financial management aspects of each proposal or report, and is mandated to request clarification on the financial management sections, recommend additional financial management assessments, request independent external audits, and propose steps for bringing a country in full compliance with this policy.

The audit requirements will vary depending on which group the country is placed in under its FMA:

Group I countries: GAVI is likely to accept the existing financial reporting and auditing processes already in place.

Group II countries: Requirements may vary widely from strengthened financial reporting to identification of a third party (either a “third party private provider” or a “transparency and accountability focal point”) to review and validate country financial reports. Actual requirements will be determined on a case-by-case basis.

Group III countries: Requirements will likely include substantial oversight by a third party private provider and external auditing. Actual requirements will be determined on a case-by-case basis.

In addition, the Secretariat has the right to commission an additional external audit for any country at any time.

### *Early Warning System*

The Secretariat will maintain a risk model on eligible countries and their cash-based awards in order to address risk preventively. This model is derived from models used by other development agencies, and will be based on publicly available data. It will be updated on a biannual basis and will provide information on:

- (i) Total grant size;
- (ii) Amount remaining to be disbursed;
- (iii) Funds utilization rate;
- (iv) Most recent Country Policy and Institutional Assessment rating or most recent Transparency International score;
- (v) Disbursement channel for GAVI cash support; and
- (vi) Findings from previous FMAs.

*Suspension of funding*

Completion of an FMA will be a precondition to funding. Failure to comply with additional requirements established by the FMA may result in suspension of funding. In addition, the Secretariat has the authority at any time to suspend cash transfers where there is suspicion of misappropriation of funds.

## Appendix 2

### Key Issues Arising from Consultation with the Working Group

#### Fiduciary Standards

##### *Scope of this paper*

- The WG members noted the reduction in the TORs for this paper, which carved out (on the basis of available time) the undertaking of a wide review of different institutions' methodologies for risk management, and the provision of a detailed proposal on the actual fiduciary standards to be adopted (on the basis that this would ideally require both the above-mentioned review and, as a second stage, a consultation with representatives of the stakeholders (including, Annex 1 Parties, eligible Parties and the World Bank as trustee) to get a sense of the policy considerations/political tolerance when assessing the acceptable level of risk. However, certain WG members expressed the view that such a consultation may not be feasible as it would be long and difficult and very political. The WG members were keen for this paper to propose a set of standards, at least at a high level (with the details to be worked out either by the Secretariat or by external consultants who may be brought in to carry out any accreditation).
- It was suggested that a set of standards could be proposed now and reviewed after e.g. 3 years, with a wider consultation process. This would allow the process to get started as soon as possible but leave the door open for addressing the political issues at a later stage.
- Notwithstanding the fact that a wide review of different institutions is not being undertaken, a number of WG members stressed the need for the Board to be able to 'benchmark' any proposed standards against those used by other institutions.

##### *Nature of standards*

- All WG members expressed the difficulty in striking a balance between the need on one hand to set credible fiduciary standards to allow the Board to carry out its duties to safeguard AF funding, and on the other hand to carry out the AF's mandate to provide real direct access to eligible Parties (for some of whom it may not be possible to achieve the standards generally required in an international context). The AF therefore needs to find standards that are achievable, objective, comparable to what the multilaterals require, but not the same, for the national level. It was recognised that there is no easy answer to this. The particular genesis of the AF, as a 'compensation' fund, not a donor fund, was stressed.

#### Accreditation Process

##### *Overview*

- A key concern expressed was that the accreditation process should not be too bureaucratic, complicated and cumbersome. There is a need to strike the balance

between maintaining fiduciary standards and allowing countries to actually get things done.

- It is important to bear in mind the nature and capacity of the AF, including the fact that the Secretariat is not strongly manned, and the Board itself also has little capacity to undertake the accreditation process, either in terms of time or technical knowledge.
- The proposed accreditation process needs to fit with the project proposal approval process set out in the Policies and Procedures (including taking into account the Board's decision that the role of the Secretariat should be limited to initial screening of applications, even in the case of those below \$1 million).

#### *Number and identity of NIEs*

- Several WG members stated that it has been agreed by the Board that there would only be one NIE nominated by each country.
- Countries may either create a new NIE or use an existing national organisation such as a department of the Ministry of Finance or the Ministry of the Environment.
- It was noted that some areas are keen on using regional entities (e.g. regional banks) as well as national entities.
- It was noted that there may be a number of political issues arising around the choice of NIE, including: (i) some countries may be reluctant to nominate the Ministry of Finance because of the risk of non-accreditation; and (ii) there may be issues with NIEs monopolising funding for their particular department and therefore there is a need to ensure that the NIE, if not the Ministry of Finance, operates under the broader mandate of the Ministry of Finance, has the capacity to engage in the broader national policy dialogue, and will not become a parallel mechanism for channelling funding.

#### *Result of accreditation*

- It was emphasised that the accreditation process should not be couched as a 'pass/fail' process. Instead, NIEs should be invited to propose/demonstrate how they will meet the required fiduciary standards, whether themselves or in conjunction with MIEs, so that NIEs do not have to be 'failed'. The role of self-assessment by NIEs could help in this process.
- There was concern about the possibility that the accreditation process may yield a different result from those of donors' own bilateral assessments.

#### *Ongoing assessment*

- There was agreement that periodic assessments of NIEs would be required and that the Board must have the capacity to monitor, verify, manage risk, and must retain some leverage.

## Capacity Building

- The potential need for capacity building for NIEs was recognised by all WG members. However, some members noted that capacity building is a long and expensive process, and therefore there is a need to consider the extent to which this is realistic in the timescale and within the AF's budget.
- Several members noted the need to clarify whether it will be the AF or the NIE itself which will be responsible for bringing the NIE up to the required standard. It was suggested that, while the AF may be able to provide funding, this should be within an agreed process/parameters, and the NIE should take responsibility for negotiating the arrangements with the relevant provider (e.g., MIE, bilateral donor, third party) itself.
- The approach adopted for capacity building needs to be flexible. There should not be a monopoly given to a particular provider.

## Fast track/stepwise implementation

- There were differing views as to the desirability of a 'fast track' process for accreditation, or a 'phased/stepwise' implementation. Some members were concerned that this would lead to a 'light' approach to fiduciary risk. It was noted that the Board must still safeguard AF funding and has an obligation to the CMP to ensure that funds are applied properly. The risk of 'fudging' in the early months is particularly high and could have severe reputational consequences for the AF. However, other members felt that it was worth taking some risk in order to get things moving.
- If a distinction is to be made by value, it is important to consider carefully where the threshold is put. For example, it was suggested that not many projects would fall below the \$1 million threshold, but several members stressed that \$1 million is still a lot of money. One member suggested that the lower value projects may even be higher risk.
- Several members thought that in practice, the first projects were likely to be implemented through MIEs. It may also be possible to 'target' initially those NIEs which will be able to meet the required standards easily. However, this needs to be balanced against targeting those countries where the need is greatest.

## Governance

- In terms of the responsibility within the Board itself for reviewing/determining any accreditation decisions, it was noted that two sub-committees of the Board have already been constituted, with responsibility for:
  - Ethics and budget; and
  - Projects and Programmes.
- It was suggested that the Projects and Programmes sub-committee could also take responsibility for accreditation, or a separate committee could be constituted.
- It was noted that any delegation of responsibility to the Secretariat would need to be considered carefully by the Board.

## Report of the working group on Fiduciary Standards

### Background

1. A working group was created at the 4th Adaptation Fund Board meeting to look at ways to accelerate the selection by the Board of fiduciary standards, including consideration of the possible ways and means on how to implement those standards. Fiduciary standards are crucial to ensure the efficiency, accountability and credibility of the Adaptation Fund.
2. This working group, after discussion, decided to ask the Adaptation Fund Board Secretariat to prepare some documents in order to help the Board going forward at its next meeting.
3. The Board further requested the Secretariat to take into account relevant elements of the Paris Declaration on Aid Effectiveness in the preparation of these documents. This paper is a formal request to the Adaptation Fund Board Secretariat.

### Objective

4. The Board first needs a comparative benchmark of relevant institutions' methodologies and requirements to provide an overview of what others do in the area of fiduciary risk management. In this respect, **the working group asks the Adaptation Fund Board Secretariat to prepare a comprehensive report, presenting the existing approaches used today**, notably in the multilateral development banks, UNDP, UNEP, GEF, FAO, IFAD, Multilateral Funds for Aids and Malaria, Multilateral Fund of the Protocol of Montréal and the Red Cross for example. Other institutions could be studied, in particular, bilateral and regional institutions, if relevant. The different modalities of "direct access" should be considered for Parties and Implementing Entities. To this end, the Secretariat can, in particular, build on the work undertaken by the Crown Agents (CAL) paper presented to the Board at its 4th meeting and by taking fully into account the discussion and the views expressed by the Board at the time of its presentation to the Adaptation Fund Board.
5. **The Secretariat should also present concrete ways to make accreditation of implementing entities possible and to implement fiduciary management.** In particular, the report should propose a fiduciary and management system for consideration by the Adaptation Fund Board of concrete procedures to allow the Board to ascertain the fiduciary standards of applicants, required to enable them to access funding from the Adaptation Fund. The report should propose the nature of Secretariat services to be required by the Adaptation Fund Board in ascertaining the proposed standards and approving the proposals particularly in the case of direct access by the eligible parties.
6. **This report should also make an assessment of possible technical and financial implications of establishing the proposed fiduciary standards** for the proponents.
7. The report will constitute an annex to the Draft Operational Policies and Guidelines for Parties to Access Resources of the Adaptation Fund and shall also provide operational text on



fiduciary standards that can be incorporated into a revised version on the named Draft.

8. The report shall be ready by May 15, 2009.

## Adaptation Fund – Fiduciary Standards - Outline Stage II Report

The purpose of this paper is to set out a brief outline of a proposed system for application of fiduciary standards by the Adaptation Fund (AF) for discussion purposes.

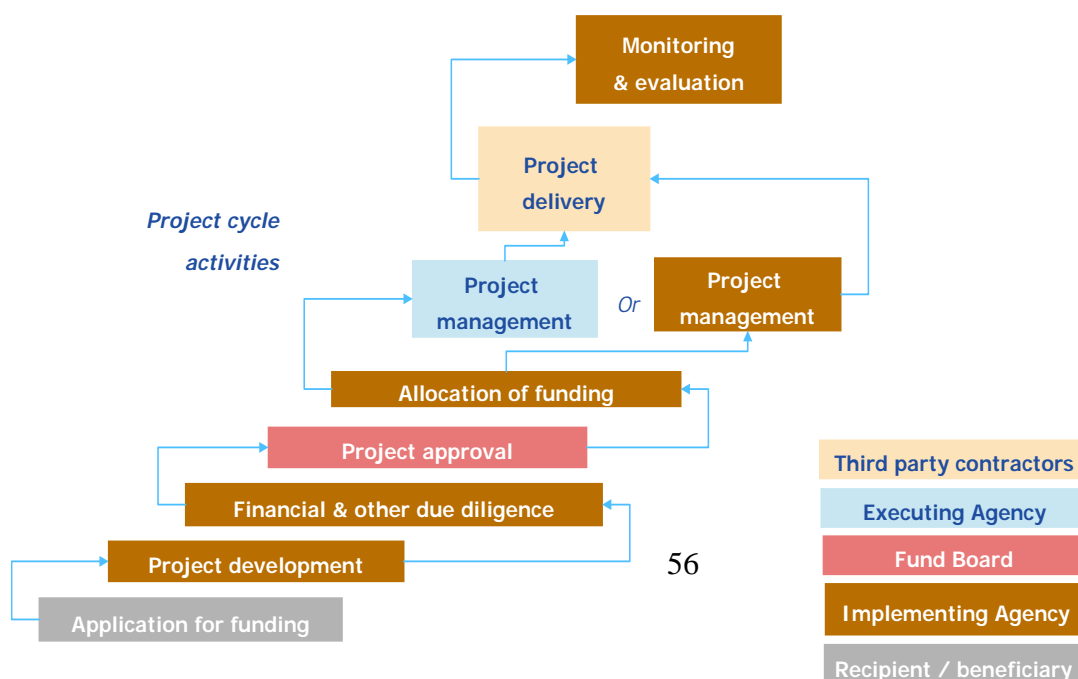
### TOR

CA Legal/CEPA have been asked to undertake the tasks outlined below.

- outline description of the accreditation process;
- outline proposal on the nature of Secretariat services required by the Board in carrying out:
  - (i) the accreditation process; and
  - (ii) the process of approving proposals in the case of direct access;
- outline proposal on mechanisms to assist Eligible Parties to access resources if their nominated national implementing entity does not fully meet the required fiduciary standards including the following possibilities;
- outline proposal on arrangements for performance management and actions to be taken in cases of non-compliance (which would not have been fully tested against stakeholder policy concerns); and
- outline assessment of possibility of a phased/stepwise implementation of the proposed fiduciary standards system.

### Implementation and Execution

In the CA Legal/CEPA paper on Elaboration of Fiduciary Standards for Implementing Entities (the CAL paper) we provided a definition of “Implementation” and “Execution Functions” for AF funded projects which are graphically illustrated in the diagram below.



We also described the role of the international financial institutions (IFIs) in the implementation which typically involves a financial/fiduciary role in terms of managing funds – typically in trust – centrally, developing and approving projects and monitoring their results. This is typically termed the “implementing” role. IFIs are often also responsible for “executing” projects, which involves the procurement of expertise and other services, and “task-managing” a project.

Although many recipient countries are relatively used to “executing” projects, fewer initiatives involve locally-based “implementation” activities.

### **Fiduciary standards**

A detailed proposal on fiduciary standards would need to be supported by an appropriate consultation exercise which is outside the scope of this paper.

At this point the exact fiduciary standards are still to be agreed, but they are likely to be based around (a) the financial integrity; (b) project management competencies; and (c) freedom to report wrong-doing demonstrated by the organization. We would recommend that within these three groups specific attributes are chosen.

In the CA Legal/CEPA paper we provided an illustration of the “operationalisation” of fiduciary standards by AF, and noted that the selection of appropriate standards for fiduciary risk management involves not only selecting the different competencies, but also making decisions about how these will be assessed. This involves:

- (i) defining the ‘metric’ or other evidence to demonstrate competency in each attribute;
- (ii) describing the required internal supporting capabilities to manage each attribute; and
- (iii) identifying potential/required external (third party) assistance for the organisation in meeting the required level of competency in each attribute.

We illustrated this using the long list of fiduciary standards proposed by the GEF in the table set out below.

Table : [ J.1 Illustrative “operationalisation” of fiduciary standards

<b>Required standard / competence and underpinning rationale</b>	<b>Measurable output / evidence demonstrating competency</b>	<b>Supporting “internal capabilities” attributes</b>	<b>Potential for external support</b>
<b>Category A: Financial integrity</b>			
Annual accounts prepared on an internationally recognized basis which provide a true and fair view of financial undertakings	Unqualified Audit report by reputable auditor	Internal audit capacity  Establishment of an audit committee	Limited other than through provision of external auditors
Robust financial reporting / control systems capable of identifying problems such as material fraud	Favourable “Control audit” report	Documented budget policies  Appropriate staff segregation	Limited
A disclosure policy which enables identification and management of conflict of interests	Tested implementation of policy found to be robust	Availability of code of ethics	Impossible
<b>Category B: Project management</b>			
Established capability to undertake appropriate ex-ante and ex-post project appraisals	Documented examples of previous effective project evaluations	Clearly stated project objectives  Availability of handbooks on project appraisal	Major area for external support
Established competitive and impartial procurement capability to inspire confidence amongst bidders	Previous successful track record of procurement employing international procurement rules	Availability of internationally recognized procurement guidelines	As above
Demonstrated project monitoring capability which	Previous demonstration of		As above

can respond flexibly to unforeseen project changes	capability through provision of effective progress and other reports		
Demonstrated independent project evaluation capability capable of measuring project outcomes and impacts	Previous demonstration of independent evaluation capability (ie independent reports)	Availability of appropriate evaluation methodologies	As above
<b>Category C: Investigations</b>			
Ability to investigate problems arising objectively	Judgmental assessment, backed by any previous investigations and / availability of guidelines	Established team with investigatory powers.	Once identified, could be investigated by third parties
Freedom to report any observed financial or other wrong-doing	Whistle-blower policy and protections	Union protection	Difficult without commitment of organization

### **Fast track**

We propose that for smaller projects (eg below a value of USD 1 million) there should be a fast track gateway for direct access (“Fast Track”).

NIE’s would submit individual applications for project funding for Fast Track projects to the AF Secretariat.

The applications would describe how the projects would be implemented and executed. NIE’s would be required to demonstrate that they had the competency to implement and execute the project. This competency would be assessed by the AF Secretariat.

We propose that the minimum financial fiduciary standard for Fast Track projects be the provision of annual audited accounts. The other financial integrity standards for financial reporting and standards would not be required.

The AF Secretariat will review these applications and award grants for each project.

The grants would be managed in accordance with appropriate best practice for the management of grants including reporting and M&E.

### **Accreditation Process**

We propose that there should be three “gateways” to “direct access” for larger projects (eg for a value in excess of USD 1 million), “Accreditation”, “Conditional Accreditation” and IFI support as described. We have set out a brief outline of the proposed accreditation below.

National Implementing Entities (NIE) submit proposals to the AF Secretariat showing how they meet the different fiduciary standards for AF Funding.

AF Secretariat commissions a reputable advisory firm to assess whether the NIE meets the fiduciary standards (or undertakes the assessment itself eg for smaller projects).

The assessment team prepares a report on whether the NIE meets the different fiduciary standards highlighting any areas where they do not, and submits the report to the AF Secretariat.

The AF Secretariat submits the report to an “Accreditation Review Panel” (“ARP”) reporting to the AF Board.

The ARP may determine:

- (i) that the NIE meets the fiduciary standards and should be accredited (“**Accreditation**”), or
- (ii) that the NIE does not meet the fiduciary standards in all respects but may be reconsidered for accreditation if it addresses areas where it does not meet the fiduciary standards, through, for instance, relying on verifiable third party capabilities in its areas of weaknesses (“**Conditional Accreditation**”); such provisional accreditation being requiring that the applicant meets fiduciary standard (c) as a minimum.
- (iii) that the NIE does not meet the fiduciary standards and requires IFI support to implement AF funded projects (“**IFI Support**”).

If the ARP determines that the NIE should be accredited the ARP requests the AF Secretariat to confirm to the NIE that it is accredited to implement projects funded by the AF, and follows up with the NIE on applications for AF funding.

If the ARP determines Conditional Accreditation the ARP requests the AF Secretariat to confirm that the NIE has not met the fiduciary standards, and to consult with the NIE as to how third party support might be utilized to address those areas where it has not met the fiduciary standards (for instance, to manage finances or aspects of project preparation) In parallel, these discussions can cover how the required fiduciary standard might be met in the longer term, through technical

assistance support, with a view to the NIE submitting for full accreditation once it has addressed the areas where it has not met the fiduciary standards.

If the ARP determines that the NIE does not meet the fiduciary standards and requires IFI support or private sector service support to implement AF funded projects the ARP requests the AF Secretariat to consult with the NIE to procure assistance from an IFI and to address the areas where it does not meet the fiduciary standards with the a view to re-submitting an application for accreditation at a later date.

The AF would be required to complete the accreditation process within 3 months of the submission of an application that complies with the AF's published application requirements.

An NIE may appeal against a decision of the ARP in accordance with the AF appeal process.

### **Performance Management**

We have set out brief outline of an approach to performance management of accredited NIE's below.

#### *Maintaining Accreditation*

Accreditation is not a one-off, but an ongoing process.

The AF Secretariat will work closely with the NIE's to support them in ensuring that they continue to meet the fiduciary standards.

The NIE will also prepare reports their fiduciary management systems, and individual projects.

The AF Secretariat will undertake or commission a periodic eg every two years assessment report of the NIE's ability to meet the fiduciary standards, and undertake and hoc special investigations where these are necessary.

The assessment / audit team submits the report to the AF Secretariat highlighting areas where the NIE does not meet the fiduciary standards.

The AF Secretariat will the assessment to the ARP with a recommendation either (i) that the NIE should continue to be accredited or that there are areas where the NIE fails to meet the fiduciary standards.

If the ARP determines that the NIE no longer meets the fiduciary standards the ARP will request the AF Secretariat to confirm to the NIE that it is no longer accredited, and may re-submit for accreditation when it addresses the areas where it does not meet the fiduciary standards, and that the AF Secretariat will consult with the NIE on how to address the areas where it does not meet the fiduciary standards, and on procuring assistance from an IFI or other service provider to

address the areas where it does not meet the fiduciary standards with the a view to submitting an application for re-accreditation at a later date.

### *AF Funded projects*

Where the NIE is no longer accredited the AF Secretariat will consult with the NIE on the areas where the procurement of services of an IFI support or to support the implementation of the AF funded projects that the NIE is currently implementing.

### **Technical and Financial implications**

We propose to explore the financial implications of the implementation of fiduciary standards for “direct access” on the basis of assumptions (based on discussions with the AF Secretariat and AF Board members) as to:

- the volume of applications for accreditation that the AF Secretariat will be required to manage (for example for smaller countries 1 application, medium sized countries 2 applications, and for larger countries 3 applications)
- the period over which the applications will be received;
- the extent to which the existing systems can cope with the increased workload.

We estimate that the cost of each accreditation review if undertaken by a third party service provider would be between USD 50,000 and 250,000 depending on the size of the project.

We will explore with the AF Secretariat how the AF would contract and manage the services of external service providers to support the accreditation process.

### **Stepwise implementation**

We propose that in order to achieve “quick results” in an initial period IFI’s should be used to support the implementation of larger projects until accreditation is achieved.

We also propose that during an interim period consideration should be given to limiting the number of applications that may be made by country in order to pilot the process.