



Jørgen Schytte/Danida



TECHNICAL NOTE ON PROGRAMME SUPPORT PREPARATION

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List of abbreviations and acronyms

AAA	Accra Agenda for Action
AMG	Aid Management Guidelines
CA	Capacity Assessment
CABRI	Collaborative Africa Budget Reform Initiative
CD	Capacity Development
CFAAs	Country Financial Accountability Assessments
CPIA	Country Policy and Institutional Assessment
GBS	Guidelines on the provision of Budget Support
GPM	Guidelines for Programme Management
IMF	International Monetary Fund
JFA	Joint-financing Arrangements
MTEF	Medium-term Expenditure Framework
MoU	Memorandum of Understanding
MoF	Ministry of Finance
NAO	National Audit Office
OECD/DAC	Organisation for Economic Co-operation and Development/Development Assistance Committee
PAF	Performance Assessment Framework
PBA	Programme-based Approaches
PEFA	Public Expenditure and Financial Accountability
PERs	Public Expenditure Reviews
PFM	Public Financial Management
PSR	Public Sector Reform
PRSP	Poverty Reduction Support Programme
ROACH	A Results-Oriented Approach to Capacity Change
SAI	Supreme Audit Institution
SBS	Sector Budget Support
SPA	Strategic Partnership with Africa
SWAp	Sector-wide Approach
TA	Technical Assistance

INTRODUCTION

This note accompanies the 2009 version of the Guidelines for Programme Management (GPM). The most fundamental change in programme management implied by the GPM is the introduction of the principle that sector budget support (SBS) is now the default modality of Danish sector (and thematic) programme support to the public sector. This is the consequence taken by Danida of the donor commitment in the Accra Agenda for Action (AAA) to make maximum use of country systems.

With a starting-point in the GPM, the note provides the Representations and other concerned parties with additional guidance for the preparation and formulation of support programmes based on the principle that SBS is the default modality.

The principle of using SBS as default covers the so called traditional sectors as well as the inter-sectoral and broader thematic areas (such as governance, agriculture, environment). The note therefore applies to all these cases.

Some of the implications of the principle are that:

- the ten budget support principles now form part of the programme support preparation process
- the risk identification and assessment becomes more systematic than before
- those responsible for programme support preparation need a more thorough knowledge of the partner country systems than has been previously necessary.

The note opens with an introduction (part I) to a number of important questions to consider when preparing a support programme in a situation where SBS is the preferred modality. The following part (II) refers to particular elements in the GPM that may present challenges in connection with programme support preparation and provides guidance for how to address these.

The order of the sections does not reflect their importance but simply follows the steps in the preparation process. Each of the sections can be accessed via a link in the electronic version of the GPM.

The note is meant as a living document that can be improved at any moment. For this to happen, the readers are requested to kindly feed back their experience, comments, and suggestions to TAS and KVA as they use the note.

1. GENERAL INTRODUCTION TO SECTOR BUDGET SUPPORT AND OTHER MODALITY-RELATED CONCEPTS

This section briefly outlines a number of questions that typically arise when SBS is being considered and describes Danida's primary position with regard to these issues.

1.1. What is sector budget support and why and when to use it

The main elements of sector budget support

OECD/DAC defines budget support as *non-earmarked donor funds being channelled to the partner government's national treasury, and thereafter managed in accordance with the partner's own budgetary procedures.*¹ This definition also covers sector budget support. Earmarked support therefore is not defined as (sector) budget support, even if the funds are managed based on the country's own procedures.

Budget support, however, is more than a mere transfer of funds. It is a package that consists of several elements - and it is the combination of these elements which is the key to achieving the results of budget support:

- The funds
- Policy dialogue - continuous - on critical development issues
- Conditions regarding policies, reforms and budget allocations
- Monitoring of performance and progress (including in poverty reduction)
- and often, support for capacity development.

Both general and sector budget support include these elements. But where general budget support and sector budget support differ is in the focus of the dialogue, the conditionality, the monitoring, and the capacity development: The focus in case of general budget support is on the overall policy and budget priorities; the focus in case of sector budget support is on sector-specific or thematic concerns.

There are no differences on the financial element; the two types of budget support use the same funding mechanism, and the only difference may be if in the case of sector budget support the donor requires *additionality* (this is explained in section 4). The term *notional earmarking* has been developed to indicate that although neither GBS (Guidelines on the provision of Budget Support) nor SBS can be earmarked in the traditional sense of being traceable (through separate accounting and reporting), SBS is intended to support the development of a particular sector based on its strategy and associated budget.

But the distinction between general and sector budget support is not clear-cut. Under SBS, the dialogue, conditionality and monitoring can also focus on overall and cross-cutting issues such

¹ OECD/DAC: Harmonising Donor Practices for Effective Aid Delivery, Vol.2: Budget Support, Sector Wide Approaches and Capacity Development in Public Financial Management. DAC Guidelines and Reference Series, Paris 2006. As amended by the Working Party on Statistics in 2008.

as public financial management or public sector reform - and under GBS the performance of particular sectors is often an important basis. Therefore the two might also be seen as two ends of a continuum:

On GBS, see the Guidelines on the provision of Budget Support at the AMG (Aid Management Guidelines) site: [\[link\]](#).

Why SBS as default? Risks and benefits

Budget support - both GBS and SBS - is generally the most aligned aid modality: Since the funds are not earmarked, the budget-allocation decisions are left entirely to the partner government so the funds can be spent entirely in line with its policies and priorities. The national ownership behind the interventions, funded by the SBS, is expected to increase the chance that the desired developmental results and impacts will be achieved. And since the donor funding is merged with the country's own funds, no other rules and procedures other than the partner country's own determine the management of the funds, including the relationships of accountability (e.g. between the Executive and the Legislative and between the sector ministries and the ministry of finance) that other modalities tend to compromise. This reduces transaction costs in the short-term and increases the chance of achieving sustainability in the long term.

Donors often see budget support as too risky because of the weak quality of the country systems: The PRSP (Poverty Reduction Support Programme) or the sector strategy may not clearly indicate the national spending priorities or results to expect. The capacity of the sector ministry or the districts may be too weak to ensure quality service provision in remote areas. The sector's monitoring system does not provide regular or reliable information on the achievement of all important targets. The integrity of the procurement system is questionable.

But the "less aligned" aid forms also carry substantial risks and costs: Earmarked support weakens the role of the parliament since it is not subjected to the parliamentary resource allocation and control mechanisms. It tends to distort the balance in the sector budget between different sub-sectors, priorities, and regions. When it comes as a patchwork of various tied funds it makes comprehensive and efficient planning difficult. It multiplies the donor requirements for planning cycles, reporting formats and schedules, monitoring systems, even accounting software, etc. and tends to make both management and implementation fragmented, inefficient, and un-transparent. In sum, earmarked support leads to significant transaction costs and fiduciary risks, that the support actually is spent on the expected results, are high.

Is not easy to rate the risks linked to budget support against those of less aligned aid. The types of risk are different, they fall on different actors, and some are short-term while others are long term: Generally the risks are mainly the concern of the donors while the benefits (such as simplicity, efficiency, ownership, domestic accountability, etc.) are enjoyed by the national partner. For earmarked support the donor receives the benefits (such as visibility, traceability, attribution of results, etc.) while the risks are felt by the national partners. Moreover many of the risks are seen as short term, concentrated and context-specific, while the benefits of strengthening country systems tend to be longer term and more general. In practice this has created a bias against the use of SBS.

The main shift with the 2009 GPM is that Danida gives first priority to the longer-term development benefits of the support, i.e. the development of the national policy making and implementation systems. Denmark now chooses to use the country systems unless something else can be justified that the longer-term development outcome of the support are outweighed by the risks.

What determines the feasibility of SBS?

There are two overall sets of considerations to make when deciding for or against sector budget support. These are

- the nature and composition of the sector
- the 10 budget support principles

Each is described in turn below.

The nature and composition of the sector - public and private, checks-and-balance actors

SBS is the most straight-forward approach to apply when the sector is dominated by a single lead agency with a specially designated (often major) envelope in the national budget (health, education, etc.), and a simple sector coordination mechanism. The advice presented in this note can most easily be used for SBS towards such "traditional" sectors.

However many sectors and thematic areas have a strong inter-sectoral character, and are made up of a mix of different actors, or "sub-sectors", often public and non-public, and in some cases with autonomous actors within the same sector. Examples of the typical "multi-actors" sectors are shown in table 1. Deciding the focus and scope of SBS to the cross-sectoral and multi-actor sectors is less straight-forward than for the traditional sectors. Even so, the principle of maximum possible alignment also covers the multi-actor sectors and SBS is therefore also in these cases the primary modality to aim for.

Table 1: Examples of multi-actor and "diffuse" sectors

Sector/thematic area	Entities participating in the sector
Agriculture	Ministries, research institutions, etc. in the public sector; farmers' associations, individual farmers, input providers, processors, financial institutions, etc. in the private.
"Business sector"	Ministry of trade and industry or similar; companies, banks, business development service providers, trade unions, industry associations, etc..
Environment	Ministry, agency, etc.; manufacturers' association, companies, NGOs, etc.
HRD	Ministry of justice, judiciary, human rights commission, etc.; NGOs, legal service providers, association of lawyers, etc.
Public sector reform, decentralisation	Ministry of public service, Civil service Commission, Ministry of Finance, Ministry of Local Government, Decentralisation/PSR (public sector reform) coordination units, line-ministries, etc.

When considering SBS for the sectors or areas listed in the Table 1, the first point of attention should be on any national strategy or sector coordination framework in place for the sector or area. A national coordination mechanism is particularly important for the inter-sectoral and multi-actor sectors or areas to ensure that they are supported in a coherent way. The starting point for Denmark should therefore be to participate in and support these mechanisms wherever they are present. Where a joint-donor arrangement is already in place, Denmark should generally participate in this and support the joint-positions of the donors as opposed to promoting more exclusive Danish priorities or support areas.

Where a sector coordination framework is not in place, the Danish focus should be turned towards supporting the establishment of this jointly with Government and other donors. This should include support towards defining a national strategy or programme and the coordination mechanism itself. The medium or long-term aim should be to put in place the conditions for making SBS possible.

There are certain typical challenges involved in tailoring SBS to the multi-actor sectors and areas which must be addressed:

- The cross-cutting sectors or areas may not be defined with a clear budget line in the national budget and the MTEF, and it is not always evident who among the different actors is best placed to lead the sector in the budget negotiations with the Ministry of Finance (especially for the governance sectors). It is therefore key that the coordination mechanisms are designed in a way that preserves the mandates and independence of any autonomous organisations in the sector, by protecting their budgets and does not introduce a power relationship that is inconsistent with the formal institutional relations between the actors in the sector. There is no standard model to follow and the exact modalities will always have to be worked out on a case to case basis, based on the local dynamics (refer to the justice, law and order sector in Uganda for an example where a working arrangement has been found).
- The right balance must be struck between a programme that is neither too narrow nor too broad, which is a challenge within multi-actor and cross-cutting sectors (whether agriculture, environment, or governance). Here the principle of "one strategy/one organisation" is not meaningful. The approach should be to view the sector as a set of linked pillars or sub-programmes which together forms the sector and contributes to the national objectives. The Danish support should then include support to 2-3 of such sub-programmes that each follows the principles for maximum alignment.
- It must be decided which sub-programmes or pillars to support within the sector or area, as well as the question of whether to support the central and/or the local level organisations that make up the sector. There is no standard answer to this question which must be addressed strategically from case to case. The important considerations are which (mix of) entities are in principle best placed to promote a coherent development of the sector by way of their mandates and functions, and which stakeholders are the drivers or spoilers" of change, when looking at the realities of interests and power. The stakeholder analysis outlined in section II can help assess the latter question.

Some of the sectors include non-public actors, but SBS (like GBS) can by definition only be used for support to the public sector. If non-public entities work on contracts with the public sector - e.g. providing goods and services to the public sector or services on behalf of the public sector- these will also benefit. But civil society organisations, private sector entities, the press, etc. are usually best supported directly and not through the government budget and SBS. Neither can SBS be used to support such public entities that are outside the government budget, such as public companies and some semi-autonomous agencies. Even if the non-public entities are part of the government's policy or strategy for the sector or area, they may not and often should not be supported through funding that is channelled via the government..

But support to non-public entities (and public entities outside the government budget) should - according to Danish policy - still be given in the best-aligned way possible, which means "core funding" should be used where possible, i.e. non-earmarked funding to the organisation against its (ideally, medium-term) plan and its programme of work. Core funding is the equivalent of budget support and has similar benefits (strengthening of the internal accountability relationships, rational allocation of resources, administrative efficiency, etc.) - but also similar challenges. It requires certain preconditions to be met, similar to the ten budget support principles (see below). The quality of governance is often a larger problem in these types of organisations than in the public sector, hence the importance even here of modalities that support improved governance, as does highly-aligned aid.

Whether SBS is appropriate for the public-sector entities of the sector/area is determined in each case by the considerations in the next paragraphs.

The ten budget support principles

The ten budget support principles describe important issues to consider when assessing whether general budget support is feasible. They cover questions of governance, poverty reduction, public financial management, and partnership, and they point at potential risks to assess when preparing for and providing budget support. The GPM section 2.3 describes how to use the principles in the case of SBS, and it is further explained in this note (Part II, section 2).

For Denmark the three most important aspects to consider in the case of sector budget support are:

- a) the policy and planning framework for the sector,
- b) the monitoring system (as relevant to the sector), and
- c) the PFM (Public Financial Management) system.

These are briefly presented in the following sections.

a): Partner programmes/the policy and planning framework. SBS like GBS is a programme-based modality, i.e. it supports the implementation of a government programme in its entirety. The existence of a partner programme therefore is a precondition for SBS; it makes no sense to finance consecutive annual budgets if they are not linked together by clear longer-term development considerations.

It goes without saying that two essential feasibility aspects of a programme are the ownership by key stakeholders (which may be several) to the programme and the capacity available to implement it.

The programme may take various forms: It could cover a whole sector (e.g. health), a sub-sector (e.g. primary health), or in some situations a single organisation (e.g. the Ministry of Health) if this is the largest entity that has a consistent *programme*, if it plays a sufficiently important role in the sector, and preferably if it may be expected to take an active part in the process of setting up a wider programme that can reduce the fragmentation in the sector. The programme may also cover a thematic area rather than a sector, e.g. a decentralisation reform programme or a reform of the enabling environment of the private sector. Or the programme may in some cases cover one or more particular sub-national governments.

In any case it is important that the programme is more than just a sequence of annual budgets. It should have some form of medium-term framework intended to operationalise one or more policies by setting out such elements as development objectives, priorities for action, targets to be reached within specified periods, outputs to be produced, activities to be carried out, a cost estimate, a financing plan, a detailed budget, a performance measurement/monitoring framework. Some of these elements may be presented in a medium-term planning document (a "strategy", a "plan", a "strategic plan", a "programme", etc.), while others are usually presented annually in work plans and budgets.

b): The monitoring set-up. There must be a possibility to monitor the progress of implementation of the programme and the achievement of the planned outcomes supported through SBS. This is because with SBS (and other programme-based modalities) the donor focus and partner dialogue shifts from inputs to the results, leaving the nuts and bolts of the implementation process to the national partners. The attention should not be on keeping track of the resources down to specific budget lines and activities (which is impossible in budget support) such as with stand-alone projects.

Therefore the existence of some sort of monitoring system is a precondition for providing SBS. Often, however, the quality of monitoring systems linked to programmes is a weak spot in countrywide systems, and there will often be a need for capacity building in this field before or even during the provision of SBS.

c): Public financial management (PFM). A PFM system of a certain quality standard is the third essential element for budget support to be possible. Yet, still more often the quality of the PFM systems is not the main barrier for budget support. Firstly, this is because the PFM systems in the partner countries have improved more over the past few years than for instance the quality of the programmes and monitoring systems. Secondly, the quality of the PFM can be measured in a relatively standard way through the internationally recognised tool, the PEFA (Public Expenditure and Financial Accountability) assessment tool: [\[link\]](#).

The PEFA assessment therefore is normally the first entry-point for assessment of the PFM system. Although a PEFA assessment does not assess risks, it provides useful pointers to the sources of PFM-related risks and is therefore the essential tool in the identification and assessment of fiduciary risks related to budget support. PEFA assessments are gradually replacing the earlier CFAAs (Country Financial Accountability Assessments) and various other

assessment tools in all of the Danish programme countries and can be expected to be carried out regularly.

However, the PEFA indicators do not cover sector-specific issues in a systematic way. Therefore, sector-specific assessments of certain PFM parameters must usually be carried out during the preparation of SBS (if they are not already available e.g. from other donors). There are good examples of such assessments – see Section 2 (para. on principle 8) in part II of this note.

1.2. Designing Sector budget support - tranches, conditions, agreements, performance assessment

The design of SBS can suitably be based on the practice and experience of Danish GBS. These are outlined as follows:

- The GBS is usually provided as two fixed tranches, disbursed together once a year: A ‘tranche A’ of minimum 80% of the annual disbursement based on a broad assessment of performance (in macro-economics, in poverty reduction, and in PFM) and a ‘tranche B’ of at most 20% based on the performance of a few specific indicators, usually governance related. Tranche B can only be disbursed if tranche A can. This ensures high predictability since at least 80% is disbursed under normal circumstances - but also enables signaling regard to particular priorities.
- The explicit indicators which trigger the release of tranches A and B are usually contained in a Performance Assessment Framework (PAF). But in addition to the PAF indicators the Danish GBS is normally conditioned on a few general “underlying assumptions”, typically concerning human rights, democracy, etc. The breach of these can lead to the interruption of support, regardless of other aspects of the performance.
- The two-tranche design can be used regardless of how other donors making up the GBS donor group design their GBS. What is important is that there is a joint PAF containing the performance indicators used by all participating donors, that the PAF has a modest number of indicators, that as many as possible of the indicators are shared by the donors, that no donor uses indicators not listed in the PAF, and if possible that the indicators used as disbursement triggers for tranche B are also used as triggers by other donors and can therefore be assessed jointly with them. (Note: however that each donor will always retain its freedom of decision in regards to disbursements.)
- In order to further increase the level of predictability, the assessments made in year n (on the basis of performance in year n-1) lead to disbursement decisions concerning year n+1. Otherwise, there is no possibility for the government to budget correctly.

Danish SBS has primarily been provided as one annual tranche only. Typically it has been based on a general assessment of sector progress and usually without reference to a formal PAF or similar.

However many donors are now increasing their interest in SBS (partly to the detriment of GBS) which makes it likely that joint-donor SBS arrangements will more closely resemble the designs of GBS. Denmark should remain flexible as to the design of SBS and promote joint

designs that are as rational and simple as possible from the point of view of both the partner government and the donors.

There is no fixed or clear recipe for how to design SBS, but depending on the circumstances Denmark should design SBS based on the following approach:

- Take as a starting point the local context and the specific nature and challenges of the sector or area. Consider the dialogue forum in place for the sector or area and turn the focus and resources towards using the opportunities that provides for an effective dialogue. Also use any opportunities in the more overall dialogue forums on GBS to raise strategic issues of the sector or area when relevant, especially if no sector or area specific dialogue forums exist.
- Include the following “underlying assumptions” in the governmental agreements, and as far as possible in the joint MoUs or similar documents underlying the SBS: Macroeconomic stability (under normal circumstances the country is on-track with the IMF); satisfactory general poverty reduction efforts (a positive conclusion by the annual PRS review); satisfactory development in PFM quality (positive conclusion by annual PFM reform review or progress/status quo in PFM quality according to PEFA assessments). Usually the “underlying assumptions” should not be evaluated explicitly, but where there is doubt if they are met they should be discussed with the government on the continued provision of SBS.
- Include in the agreements the option to split the support in a tranche A (released following an overall sector performance that is positive) and a smaller tranche B (released following the positive performance on one or a few selected indicators of particular importance). The decision to split could be annual, depending on whether there are particularly critical issues that Denmark would like to highlight to the government. Note however, that tranche B triggers should usually not be outcome indicators as these do not depend on government action only, but rather indicators referring to policy or reform measures agreed with the government, to improvements in important processes, to outputs, or to inputs.
- The already mentioned method to secure the predictability of the support - years $n-1$ (object of assessment), n (year of assessment), $n+1$ (year of disbursement in consequence of the assessment) - should apply.

The above three elements can be built into Danish SBS programmes regardless of how the other donors’ support is designed. However the timeframe and way to go about the next (last) element depends on the actual circumstances in each case.

- A formalised sector/thematic performance assessment framework to increase the transparency and clarity as to the basis on which the sector performance is assessed and to facilitate the harmonization among donors in this regard. The frameworks should be “co-owned” by the government and the donors and normally contain two sections: One including a set of selected outcome indicators (defined for a multi-year period) and another (often defined annually) including relevant input indicators (budget allocations,

actual expenditure) and indicators referring to policy- and reform-related measures to be taken by the government.²

If it becomes relevant to include a condition on input (financial) *additionality*, this could be done by including the government's sector funding in the general assessment of sector performance under tranche A, or in the conditionality related to tranche B (refer to section 4). Whatever the solution input additionality is difficult to measure and failure to show additionality in a single year usually does not justify any interruption or reduction of the sector budget support. Such failure can arise for good reasons, for instance in the case of emergencies that put extra budgetary stress on the government, or the sector facing particular constraints in its implementation capacity.

Additional considerations relating to conditionality, PAFs, reviews, etc. that are applicable to SBS are found in the Guidelines for the Provision of General Budget Support, Chapter 5: [\[link\]](#).

1.3. The Reporting requirements of SBS

The MoU (Memorandum of Understanding) or JFA (Joint-financing Arrangements) should specify the progress and financial (including audit) reports to be produced by the partner government. If it does not, the reporting requirements must be specified in the Government Agreement.

In analogy with GBS, the minimum requirement is comprised of the following reports:

Progress reporting

- Annual progress reporting on the implementation of the sector programme, including available information from the sector monitoring system and ad hoc studies on achieved outputs, outcomes and impact.
- Annual reporting on the implementation of specific measures and achievement of specific targets agreed in the PAF or similar.
- Annual State budgets and up-dated Medium-Term Expenditure Framework
- Any diagnostic studies, assessments or reviews of relevance to the SBS, e.g. PEFA assessment, Public Expenditure Review, Public Expenditure Tracking Study

Financial reporting

- Regular reporting on in-year budget execution in the sector
- Annual State Accounts for previous financial year as presented to the national legislature. Should include on the revenue side the SBS received from each individual donor
- Annual account statement on the flow of SBS into the central treasury account, including confirmation of receipt of SBS in foreign currency by the central bank as well

²See for instance [\[link\]](#) to PFM-Study of the health sector of Mozambique in 2009.

as proof of exchange and the corresponding amount in local currency credited to the national treasury

- Letter of confirmation of SBS received after each disbursement by the Representation, specifying the amount received in foreign and local currency

Audit reports

- The annual report from the national audit office (NAO) on the audited state accounts as presented to the legislature.
- The legislature's formal comments on the annual audit report
- Annual audit report verifying the flow of funds from the foreign exchange account to the central treasury account
- Regular performance or value-for-money audits of samples of sector activities.

1.4. Additionality - what it is and how to work with it

The basic premise for providing GBS or SBS is that it leads to "additionality" - i.e. that something happens or changes as a result of the SBS that would not otherwise have occurred. During the programme preparation process special focus should be placed on making sure that the support leads to "additionality".

Additionality can be looked at from the input side (additional funding) as well as from the results side (accelerated development). The two are closely related, but for Denmark what is ultimately sought in all cases of SBS (as in any support) is obviously the results-side additionality.

There are various ways to promote results-side additionality through SBS. SBS allows the representation to take an active part in the sector dialogue and place the spotlight on the constraints that need to be tackled, before increased sector funding can be productively spent. Although funding tends to be a universal problem, under-funding is not always the most acute development constraint in a sector: Inefficiency, ineffectiveness, an inappropriate balance between recurrent and investment expenditure or between sub-sectors (such as primary education as compared with secondary and tertiary education), slowness of sector reform, low budget execution rates, or human capacity gaps, etc. The dialogue around the SBS should focus on reducing such constraints, and it can be accompanied by Technical Assistance (TA) and/or earmarked support addressing some of the most critical constraints.

The quality of the performance assessment framework for the sector or area is therefore central to the ensuring results additionality; here the jointly agreed results are defined, indicators and targets, which the dialogue on results can focus on. This underscores the importance of emphasizing the monitoring framework in the assessment of the 10 budget support principles.

In practice, it can be difficult to demonstrate financial additionality in an objective and precise manner. The question of whether input additionality should be a requirement for the support will need to be determined as part of the identification of the constraints and challenges in the

sector together with the government and other stakeholders. The main issues to be raised in the dialogue and included in the conditionality will have to be identified. If under-funding is one of these issues, input-side additionality may be relevant as a condition to the government.

Demands to a partner government that a sector each year should receive exactly the Danish amount of support (or more) in addition to other budget allocations should therefore be avoided. Instead the representation should - in close cooperation with other donors - focus on avoiding that the Danish/donor contribution is met with a withdrawal of government funding from the sector. A single year not living up to the condition should however not automatically result in sanctions; rather, the government should be asked to explain the reasons which must then be discussed and assessed by Danida/the donors before possible consequences are taken.

The steps to formulate a condition regarding financial additionality would be the following:

- seek to establish the amounts of domestic and total funding for the sector over the past few years as well as the growth of the total government budget (look at both budgeted amounts and actual expenditure in order to capture the intentions as well as the execution);
- look at the projected domestic and total sector funding as well as the projected total budget over the period of the medium-term expenditure framework (MTEF);
- on this background, determine a feasible minimum requirement to the government (usually in terms of actual expenditure rather than budgeted amounts) regarding its future domestic funding of the sector.

Note that regardless of the circumstances of the sector, the funding situation and its development over time should always form part of the donors' *monitoring* of the sector. The first two of the above bullet points indicate some of the main elements in this.

1.5. Difference between SBS and earmarking

By definition SBS is not and cannot be earmarked in the traditional financial sense: Once the funds are disbursed to the Treasury, their flow through the financial management system cannot be traced. They may be used for any purpose allowed in the national budget.

Even so, the funds can be said to be "notionally earmarked" in the sense that they are intended to support (or "targeted towards") a particular sector or thematic area in support of the government's objectives for the sector or area.

But for donor funds that are notionally earmarked there is no requirement for governments to produce specific financial reports or audit reports. In fact notionally earmarked funds cannot be accounted for specifically. With notional earmarking government is required to produce and share with the donor the budgets, financial reports, monitoring results, progress reports, and audit reports for the sector as a whole, regardless of the sources of funding.

Unfortunately, the terms are not used the same way by all. In this note, "traditional" or "financial earmarking" is used in the sense that funds can be *traced* whereas "notionally earmarked" support is untraceable. In this sense the term "earmarked budget support" therefore is meaningless.

Others take “earmarking” to mean “targeting” in a broad sense, including also “notional earmarking”. In this sense “earmarked budget support” is a more meaningful term. Even other versions are seen from time to time. In discussions, care must therefore be taken to specify what is meant by the various terms.

1.6. When SBS is not possible: How best to use earmarked support

Sector budget support should be the first option to consider when designing Danish support - at least when it targets public sector entities on the government budget.

If SBS turns out not to be possible, various options of “earmarked support” will need to be considered. This will be the case when the assessment points to reservations that cannot be addressed through mitigating measures that are compatible with SBS.

“Earmarked support” can be designed in ways ranging from highly-aligned to more or less non-aligned support. The alignment commitment means that the highest possible level of alignment should be identified and used in each case where SBS is found not to be possible. To this end it is necessary to determine precisely the factors that make SBS unfeasible: Which preconditions are not met? Which risks are not acceptable to Danida? Or which other considerations need to be taken into account? – see the following section.

- E.g. is the problem lack of a consistent or realistic government programme for the sector/thematic area, or lack of a working monitoring system, then the government’s PFM system may still be used - and the support should include capacity development support to address the weak areas identified.
- If the problem lies with the procurement system - and sample-wise procurement audits are not seen sufficient as a safeguard, then some kind of donor involvement in the procurement process can be introduced and the rest of the PFM system could still be used.
- If the national audit authority cannot be relied on, all other aspects of the PFM system can in principle still be used. Etc.

Many countries have introduced procedures that allow full use of the national PFM system (except the above-mentioned allocation-related mechanisms and possibly auditing), even for earmarked support. Here, apart from an “earmark” in the form of a particular digit in the accounts code which allows the generation of specific financial reporting and auditing, the donor funds are treated like domestic funds in the national system. This reduces the cost of administration considerably compared to situations where various donor requirements have to be honoured by the partner government.

The level of alignment to the partner country’s PFM system can be chosen if one identifies the maximum level of alignment in each of the stages of the annual budget process separately - planning, budgeting, parliamentary approval, accounting, reporting, auditing, etc.³

³See “Putting Aid on Budget. A Study for the Collaborative Africa Budget Reform Initiative (CABRI) and the Strategic Partnership with Africa (SPA)” from 2008 that can be downloaded from the two organisations’ website: [\[link\]](#).

But earmarked support can only be partially aligned. The common feature among them is the fact that the project or programme agreement already states the use of the funds and thereby cuts the national resource allocation process (involving in particular the ministry of finance, the cabinet, and the parliament) out of the circuit, thus reducing the role of important domestic accountability relations which in their turn are fundamental for the quality of governance. Clearly, this is already an essential deviation from total alignment, drawing a clear borderline between budget support and earmarked support.

1.7. How SBS and earmarked support can complement each other

There are three types of justification for not using sector budget support in all cases.

- Where basic preconditions for SBS are not met (most frequently nonexistence of a relevant partner programme and/or of a monitoring system)
- Where the risks associated with SBS cannot be managed satisfactorily within the modality of budget support itself (i.e. by way of mitigation measures that are compatible with sector budget support).

This note gives most attention to two situations above. In these cases the support needs to be earmarked, using the country systems less than fully. It may not necessarily reflect a wish to target the funds more narrowly than in SBS, but rather to be able to trace the funds and to control that they are being spent in accordance with intended purposes and expected standards.

The third type of justification is about cases where other aid instruments may by nature be more appropriate than SBS:

- Where the support concerns technical assistance, large-scale infrastructure projects, pilot projects testing innovations, and funding of transitory and narrowly defined activities. This list is indicative and the categorisation of an activity as non-eligible for SBS due to its nature must be made and justified in each case.

2. ISSUES IN PROGRAMME SUPPORT PREPARATION AND FORMULATION

This part of the note supplements the GPM by advising on how to address the elements in the sections of the GPM that deal with SBS.

The overall steps described are stakeholder (political economy) analysis, assessment of the 10 budget support principles, risk assessment - and weighing these assessments against each other to reach the conclusion on the feasibility of SBS.

The section is not meant to be read as one continuous text and only covers certain aspects of the programme support preparation process.

THE PREPARATION PHASE

2.1. Analysis of sector/thematic area – stakeholder analysis

The aim of this step is to get a good understanding of who are the key stakeholders which will play a role, positively and negatively, in ensuring that the programme goals are achieved - and what are their interests and levels of influence (power) in helping to achieve the goals.

As part of this it is important to assess the level of ownership of these stakeholders to the programme supported. Note that often there can be several stakeholders on the government side with differing interests and that non-government stakeholders (incl. private sector) may also be important to consider.

Such "stakeholder analysis" is an aspect of "political economy"-type analysis, which is now a guiding principle that should underpin the preparatory assessments of Danish support. This is defined in the Danish public sector management strategy *Effective and Accountable Public-Sector Management. Strategic Priorities*: [\[link\]](#).

The rationale for giving attention to understanding the political economy, interests and power relations is the well-known fact that change processes - such as reforms, capacity development, and development generally - is as much a political as a technical process; the most rational development path in a technical sense is not necessarily the most optimal in a political sense and vice versa.

Go through the following steps to undertake the stakeholder analysis:

- Use political economy or stakeholder analysis first and foremost in programme preparation (in particular where reforms or other major changes are on the agenda).
- Use such analysis for two alternate purposes, namely to understand how and which overall economic, social and political factors affect the adoption, content, and implementation of change with the development programme, and/or which stakeholders in relation to the programme to support and engage with in particular, how to focus the policy dialogue, and why the process - such as the design and the implementation of the sector policy and strategy - takes the course it does. Such understanding can be used to help define the right risk mitigation measures and make the expectations related to the implementation more realistic.
- Consider and define the exact purpose of the analysis carefully - i.e. whether to focus on broader drivers of change related to the sector or more directly on the stakeholders engaged in the sector or area and their interests and power relations
- Based on the purpose, consider carefully which among the several tools available that can be used for this purpose, and decide on the scope and complexity of the analysis; the analysis can be more or less thorough and lengthy, depending on the complexity of the sector and the importance of in-depth knowledge of the situation, and weighed against the financial and transaction costs caused by the exercise. Some elements of the tools for stakeholder analysis are summarized in box 1 below.

Box 1: Typical elements of stakeholder analysis

Stakeholder analysis - typical elements:

- identification of the stakeholders
- identification and assessment of
- their interests or objectives (formal and informal)
- their importance for successful change
- the importance they themselves attach to the change process in question (their incentives),
- their strength, i.e. their power to influence the process
- Rating of (some of) the above parameters for each stakeholder on a simple scale.

Mappings of the stakeholders along the lines of these and other parameters can be made in more or less sophisticated ways and can yield useful knowledge on the landscape of forces for and against the intended change and thereby on the constraints and potentials to take into account. Note that stakeholder analysis is qualitative, and it needs to build on information that is rarely written down.

Good sources of inspiration for commissioning a stakeholder analysis include the World Bank PSIA (Poverty and Social Impact Analysis) Source Book [\[link\]](#).

the instrument called "Stakeholder Power Analysis" of the International Institute for Environment and Development (IIED) [\[link\]](#) , which refers to a few examples from the environment sector; and, Tools and Methods Series, European Commission, 2009 and EuropeAid's "Toolkit for Capacity Development in a sector context" [\[link\]](#) .

- Try to delimit and target the stakeholder analysis to the main components or sub-components of the sector or area supported, also considering the complexity of the sector policy/strategy/programme.
- Decide in advance based on careful consideration how to implement the stakeholder analysis. Options include a light approach where relevant questions are inserted in interviews carried out anyway as part of the sector analysis to a heavier one of arranging special group workshops where the mapping of stakeholders' interests and influences can be carried out in a more participatory way. Try to do the stakeholder analysis jointly with other donors to obtain a shared understanding and common approaches and expectations.
- Use the information from stakeholder analysis actively to develop support strategies for managing and support the change that take into account the political realities and opportunities
- Use also the understanding of key stakeholders and interests to support the dialogue process, especially by identifying the broader range of stakeholders that needs to be involved, and how and where in the process to involve them to best meet their interests to ensure they promote or do not block programme implementation

2.2. Assessment according to the ten budget support principles

The GPM asks for an analysis during the programme preparation process of the extent to which the ten budget support principles are fulfilled.

All ten budget support principles must be assessed at national level assessment - while five of the principles must be assessed at sector level.

The assessment at national level should normally be available already. It is usually part of the latest Assessment of Country Programme (which from 2009 includes a brief assessment of each of the principles separately). But if no recent assessment of the ten principles at country level is available, a new or up-dated assessment must be made as part the sector programme support preparation. Use the checklists in the Guidelines on the Provision of Budget Support [[link](#)] as inspiration, but note that the assessment for SBS does not need to be quite as comprehensive as for GBS. If needed, issue specific studies - such as a sector assessment on corruption - could be funded.

The macroeconomic situation should be assessed as part of the national assessment. If an IMF programme is being implemented satisfactorily this will in itself be seen as enough assurance that a stability-oriented macroeconomic policy is followed. The IMF, typically plays a key role in monitoring and advising on the macroeconomic framework and therefore has privileged access to government and financial sector data and information for evaluating macroeconomic risks. Close liaison and consultations with IMF missions and staff are encouraged in order to stay abreast with economic developments that might pose risks to successful programme implementation and allow for timely remedial measures, and / or contingency planning. But the absence of a programme with the IMF should not by itself be taken to imply that a stable macroeconomic framework is absent. The Representation should always assess the reasons for the status of the IMF programme and then make a judgment of whether a stable macroeconomic framework is in place. This also implies that a brief analysis and argued conclusion should be developed even if, and where, an IMF programme or facility is "on track".

The five principles that must be assessed at sector level (or thematic area) are:

- The sector/thematic policy and planning framework (#3)
- Development results achieved and documentation of these (#4)
- Public financial management issues for the sector (#8)
- Partnership situation at the sector level (#9)
- Joint-financing mechanisms/arrangements for the sector (#10)

These areas are central to SBS, and the situation of each area can usually be quite different between the national and sector level, and also between sectors.

The following sub-sections provide checklists and other information that guide the assessments of each of the five principles, but first three general points:

- Do not aim to rate the budget support principles against a fixed standard. There is not a given minimum standard below which SBS is not allowed or feasible. Use instead the assessment to get a general picture of the risks that need to be evaluated - in particular the risks that threaten to make SBS ineffective in achieving the intended development results. See the following section on the risk assessment.
- Try as much as possible to join the data-collection and analytic effort of the GBS with that of the SBS. Many of the information needs are the same, and there is considerable overlap between the GBS assessments and issues for the sector/thematic analysis, cf. GPM section 2.2.
- Draw as much as possible on information in existing documents. These include primary sources (general and sector planning documents, progress reports, impact studies, budgets, financial management regulations, etc.) as well as secondary documentation such as governance profiles, various "institutional assessments"⁴, PFM assessments (PEFA, CFAA, etc.), public expenditure reviews (PER), expenditure tracking studies, programme and project review and evaluation reports, etc. Consult any World Bank assessments with information on individual sectors, such as Country Policy and Institutional Assessment (CPIA), Country Environmental Analysis, Country Social Analysis, Strategic Environmental Assessment, Poverty and Social Impact Assessment)

Principle #3 – the sector/thematic policy and planning framework

The aim here is to assess the quality of the policy, strategy and/or programme for sector or thematic area - i.e. its policy and planning framework for the sector/thematic area, in whatever form it may take.

In fact, the nature of the documents that can be counted as making up the sector/thematic area's policy framework will vary among countries and sectors.

The quality of the policy and planning framework is essential because this defines the development goals and strategies which Danida commits to align with and support directly. Many of the risks of the SBS will be linked to the quality and feasibility of the sector or thematic policy and planning framework supported - just as the major benefits arise from the alignment to the national policies and priorities that are expressed in the planning documents.

Besides the quality of the planning framework itself, two fundamental factors that determine if the framework is realistic are:

- Whether there is capacity at all levels to implement it, which means this must be assessed.
- That there is a genuine national ownership and commitment to implement it, which should be looked at as part of the stakeholder analysis presented earlier (relating to GPM sector 2.2).

⁴ See e.g. Toolkit for Capacity Development in a Sector Context, Tools and Methods Series, European Commission, 2009.

The analysis of the policy and planning framework should enable the Representation to answer if *it is sufficiently clear what the government intends to achieve in the sector/thematic area and whether it is realistic and feasible.*

- To this end examine the following five issues and try as best as possible to respond to the questions:
- The policy, the objectives, the priorities (I.e.: Is there consistency with the national development strategy? With the national MDG commitments? With other international commitments, e.g. conventions? Is there agreement with Danish positions?)
- The technical quality (I.e.: Are the documents internally coherent? Do they present sufficiently specific and concrete outcomes and outputs? Are they realistically costed? Are they monitorable?)
- Governance issues (I.e.: Is/was the planning and priority-setting process participative and inclusive with regard to important stakeholders in the sector/thematic area? With regard to the poor? Is/will the management and implementation process be responsive to the concerns of important players and target groups?)
- The feasibility (I.e.: Is the plan/strategy realistic in view of the expected availability of funding? In view of the implementing capacity at all levels of the sector/thematic area? In light of previous experience? In light of the political and other commitment and backing?)
- The implementation (I.e.: What is the track record in the sector/area in terms of budget execution? In terms of production of outputs? In terms of achievement of outcomes? In terms of implementation of reform measures?)

Principle #4 – development results and the documentation of them

Here the aim is to gain a good understanding of the experience of development cooperation in terms of the sector's delivery on results *and* how well results are being monitored and documented for the sector or thematic area.

Specifically,

- The focus when assessing the developmental track record should be on the extent to which the sector has contributed to national poverty reduction: Have the sector policies, strategies, etc. been poverty-oriented? To what extent are they implemented to either benefit the poor directly or contribute to poverty reduction in other ways? (this overlaps with the last bullet point of the list above.)
- The focus when assessing the documentation of developmental results is on the monitoring or performance measurement system of the sector/area. This is an(other) essential element of the country systems in the context of SBS as it makes it possible to identify the results achieved, based on the entire budget and other resources for the

sector/area as opposed to activities funded specifically by the donor. Without a reasonable possibility to follow the achievement of results, SBS is compromised as a modality.

Overall the representation should be able to answer the following question:

Does the monitoring system allow the Danish Representation to follow the development and achievements in the sector/thematic area (not least in the Danish priority areas within the sector/area, if any) with sufficient detail and frequency to be assured of the benefits generated?

To answer this, analyze the following issues and questions:

- The quality of the indicators (I.e.: Are the indicators specific and measurable? Do they cover all important areas of action and all targets?)
- The clarity and realism of the targets (I.e.: Are the targets realistically achievable? Are they time-bound in a realistic way?)
- The organization of the monitoring process (I.e.: Are the involved entities relevant in view of their involvement in the sector/thematic area? Do they have the required capacity, including funding?)
- Data and reporting (I.e.: Is the data reliable? Is the frequency, comprehensiveness and quality of reporting sufficient?)

Basic information on monitoring can be found in the series of technical notes on monitoring and indicators (including brief documents on general issues in monitoring and on monitoring in a number of sectors/themes). See the Development Forum website [[link](#)].

Principle #8 – public financial management

The focus here is on assessing those requirements relating to the quality of the PFM system which concern the sector or area in particular (including the assessment of the procurement system required in principle #6).

Normally a single PFM overall system applies to the whole of the public sector (except for semi-/autonomous entities such as public companies and some agencies) - but the capacity to operate it and to comply with it, and sometimes the degree of commitment and integrity, may vary considerably between institutions.

Yet the general PFM assessments that are more or less regularly carried out do not usually capture this diversity. This for instance is the case for the Country Financial Accountability Assessments (CFAAs) of the World Bank, but also for the Public Expenditure and Financial Accountability (PEFA) assessments which are gradually replacing the CFAAs in nearly all of the Danish programme countries. Usual PEFA assessments only cover issues in specific sectors in an unsystematic way, and there is no PEFA methodology for carrying out sector-level assessments.

The following points give some guidance for assessing PFM issues for the sector or thematic area:

- Consult the various attempts at adapting the PEFA methodology to sectors; use these as inspiration if a group of sector donors together with the authorities agree on commissioning a sector-specific PFM assessment.⁵
- Examine any available PERs (public expenditure reviews), expenditure tracking studies and service delivery surveys as these can contain useful information not only on sector PFM, but also on more results-related issues. Also see if there are any more specific studies made, e.g. on the performance of the procurement system or on staff management, perhaps carried out as part of general reform programmes (civil service reform, decentralization reform, etc.).
- Any comprehensive PFM assessments should be done as joint-donor exercises, since they always cause significant transaction costs for the national authorities. Even in situations where Denmark alone is preparing programme support, it is important to gather sufficient sector-level knowledge of the quality of PFM to assess the fiduciary risks associated with SBS.
- If no sector-specific PFM studies exist, then use any recent PEFA assessment as a starting point: The weaknesses identified in the PEFA assessment will often point to issues that merit particular attention at sector level. Note however that the rating of the PEFA indicators on its own is not enough to provide the full picture; the explanations given in the report are just as important.
- A number of the PEFA indicators concern issues that are relevant to look at in more detail at sector level (see box 2 below), because their quality can vary considerably among sectors. This does not mean that sector-level assessments of these indicators against the PEFA rating should be done. But even so focus the attention on these issues as they can vary greatly between sectors. Select the exact issues to be assessed in each case.

⁵ See for instance study done in the health sector of Mozambique in 2009 [\[link\]](#).

Box 2: Sector relevant PEFA indicators

#1 and 2 on the expenditure outturn compared to the budget,

#3 on the revenue out-turn (user fees, etc.),

#4 on the volume of arrears,

#5 on the budget classification,

#7 on unreported government operations (which include donor-funded projects not reflected in fiscal reports),

#12 on multi-year fiscal planning (MTEF and similar),

#18 on payroll controls,

#19 on procurement,

#20 on internal controls for non-salary expenditure,

#21 on internal audit,

#22 on accounts reconciliation,

#23 on availability of information on resources of the service delivery units,

#24 on the availability of in-year budget reports.

- Consider giving special attention to assessing the procurement system; procurement often consumes a huge proportion of the funds available to a sector and often merits attention (procurement system is covered by PEFA indicator #19).
- Consider the relevance of assessing PFM also at local government level. In many countries, local governments play an important role in delivering services and other public functions, which makes PEFA indicator #8 (on inter-governmental transfers) particular relevant. It also indicates the importance of the quality of PFM at sub-national level(s). Consider the need and possibility of using the special tool developed by the PEFA secretariat for sub-national PEFA assessments. Normally, however, it is not recommended to do a representative assessment of PFM in the local governments of a country in a Danida-only programme support preparation process; this is usually a huge exercise. Rely instead on more cursory and selective information, based on own and other donors' experience of particular constraints.

Principle #9 and principle #10 – the partnership situation and joint financing mechanisms

The aim of this part is to assess the quality of the partnership in the sector/area and the instruments that are used to formalise the cooperation between donors and government.

Consider the following questions to assess the partnership situation:

- To what extent do the partner organizations take the lead in the partnership, including in coordinating the donors and facilitating the division of labour between them?

- What is the level of quality of the sector/thematic dialogue - and how inclusive is it (including non-governmental actors where relevant)?
- What is the level of quality of follow-up by the authorities to agreements made with the donors?
- What is the level of quality and regularity of progress and other reporting made available to the donors?
- What is the level of quality of preparation and execution of sector/thematic reviews?
- What is the level of quality of cooperation between the donors, including the existence and the agreements around a possible lead donorship arrangement?

For joint-financing arrangements (JFA) (if any) the Nordic+ template is the primary reference in cases where Danida participates.

Consider the following:

- Does the JFA cover the issues mentioned in the template?
- To what degree does the JFA fill its role to facilitate the cooperation in the sector and to structure the partnership in a productive way - does the JFA facilitate the application of highly-aligned financing modalities and instruments? Does it facilitate partner ownership? Does it facilitate a high degree of inclusiveness in the sector partnership? Is it adhered to by the partners? Etc.

2.3. Preliminary risk assessment, choice of aid modality

The assessment of the ten budget support principles should be followed up by a risk assessment.

In the end of the preparation process, the conclusion of whether SBS is feasible for the sector or area should be made by weighing the risks against the benefits of using the country systems in the maximum way, based on the perspective of achieving the intended development outcomes in the long run.

Even later in the process (during formulation), the risk assessment should be continued in order to determine which safeguards to use in case SBS is decided on - or in case SBS will not be used, what level of partial alignment to use (see section 5 and 6 below).

Therefore the aim of the risk assessment is to identify and assess the risks that relate specifically to the effectiveness of SBS, which ultimately will be looked at in terms of poverty reduction. Examples of such risks can be seen in the table. In practice, such risks are likely to concern the principles #3 to 8 more than the rest, i.e. those that relate to the parts of the country systems that SBS aligns more to than earmarked support, namely a) the policy and planning framework, b) the monitoring system, and c) PFM.

To this end do the following:

- Identify the risks based on the information used for assessing the ten budget support principles and as a natural consequence of this assessment. On PFM, however, do not take the PEFA assessments as risk assessments in themselves; PEFA gives technical information on the functioning of PFM but it does not give a value judgment on the fiduciary risks (i.e. the risk that funds cannot be accounted for, are not used as intended, or do not obtain value for money). Therefore the financial risk assessment must look beyond the PEFA assessment and draw on additional insight and information.
- Present the identified risks in a table such as table 2
- Do not include risks that affect (the effectiveness of) any form of support in the same way, such as risks associated with a lack of independence of the judiciary. The bias or arbitrariness of decisions stemming from this will be assumed to affect any form of sector support for which an independent judiciary is important, not SBS in particular
- Be specific when formulating the risks so as to be sure the statements point to ways to mitigate them. State in the last column the Representation's opinion as to whether the impact of the occurrence of a risk is insignificant / minor / moderate/ major/ catastrophic and whether the likelihood of this risk occurring is rare / unlikely / possible / likely / almost certain. There is no mechanistic formula for grading risks, but even if in this sense the assessments remain subjective, their validity obviously increases with the depth of the knowledge that is available to the Representation.
- Make use of the notes on the concepts which apply to risks and risk management and which will be useful when reading this section as well as section 5.
- Summarise the above presentation of the risk identification and assessment in an argued conclusion regarding the feasibility of choosing SBS as the modality for programme support delivery. Take into consideration that safeguards will be set up to mitigate and manage the risks that have been defined. The safeguards need not be specified at this point (Section 5 below lists examples of safeguards that are usually considered compatible with SBS).

Table 2: Risk Identification and Assessment

GBS principle	Principle (country level)	Principle (application at sector level)	Risk identification	Assessment of Likelihood/ Impact
	Governance		Are specific risks to SBS effectiveness discernable? What do the risks consist of?	
1.	Good governance, encompassing a minimum respect for human rights, a free press, pluralistic democracy and rule of law, including independence of the judiciary	n/a	<p><u>Example:</u> Weak opposition in Parliament → risk of weak oversight of Executive, biased planning, corruption in large-scale procurement</p> <p><u>Example:</u> Country recently emerged from conflict and the situation is fragile → risk that government operations will be halted/interrupted in South because of social unrest.</p>	<p>Likely/major</p> <p>Possible/minor (but catastrophic in South)</p>
2.	Anti-corruption with implementation of prevention and control measures	n/a	<u>Example:</u> Refer to Principle # 6	
	Poverty reduction policies			
3.	Solid poverty reduction strategy and the will to implement it	Sector/thematic policy and plan/strategy/programme	<p><u>Example:</u> No proper costing of sector strategic plan → risk of compromised feasibility, of “shopping list” character, of unsatisfactory real prioritisation and outturn.</p> <p><u>Example:</u> No multi-year perspective, only annual work plans and budgets → risk of no link to policy and to expected longer-term outcomes.</p> <p><u>Example:</u> Over-emphasis in sector strategy on tertiary health → risk of weak poverty impact</p> <p><u>Example:</u> <u>Vested interest against program policies and reforms from different stakeholders identified through political-economy analysis. E.g. urban middle class oppose abolition of general educational subsidies at the detriment of targeted pro-poor subsidies. E.g. Negative bias in pro-poor subsidies in water supply.</u></p>	<p>Likely/moderate</p> <p>Likely/catastrophic (This rather amounts to a lacking precondition for SBS than to a risk → postponement of SBS)</p> <p>Likely/moderate</p> <p>Likely/strong</p>
4.	Positive experiences of development cooperation generally and of budget support specifically, as well as ongoing documentation of concrete development results	<p>Previous poverty reduction results in sector/area</p> <p>Monitoring system at sector level</p>	<p><u>Example:</u> Unreliable data as basis of reports → risk of misguided implementation.</p> <p><u>Example:</u> Only progress (activity) monitoring established → risk of weak and unsystematic knowledge of wider and longer-term effects (outcomes), of relationship with policy.</p>	<p>Possible/moderate</p> <p>Likely/major</p>
	Public financial management	(all risks relating to principles 5 to 8 might as well be stated under 8)		
5.	The Finance Act process, with publication of budget and accounts, as well as parliamentary	n/a	<u>Example:</u> Min. of Finance bullies sector ministry → risk that sector priorities not well reflected in state budget	Likely/moderate

GBS principle	Principle (country level)	Principle (application at sector level)	Risk identification	Assessment of Likelihood/ Impact
	consideration			
6.	Rules for procurement broadly in accordance with international standards	n/a (included in principle 8)	<p><u>Example:</u> Procurement rules accord with international best practice but compliance is low → risk of low value for money, of corruption.</p> <p><u>Example:</u> Procurement process very slow → risk of slow budget execution, low achievement of objectives.</p>	<p>Possible/moderate</p> <p>Almost certain/moderate</p>
7.	Presence of an independent supreme audit institution or inspection body with similar functions	n/a	<p><u>Example:</u> Lack of independence of the Auditor General makes it difficult to hold key players in the sector accountable → risk of weak incentives to strengthen financial controls and general compliance with regulations, risk of continued inefficiency, loss of funds, etc.</p> <p><u>Example:</u> Auditor General has low capacity; irregular audit of sector institutions → risk of impunity, of deterioration of compliance, of increasing fiduciary risks.</p>	<p>Possible/major</p> <p>Likely/major</p>
8.	Expert appraisal of quality and capacity in public financial management	Quality of PFM at sector/thematic level (other issues than under 5 – 7)	<p><u>Example:</u> Unreliable and irregular in-year budget execution reports → actual level of expenditure not well known before end-year, risk of over- or under-expenditure, risk of skewed expenditure across sector.</p> <p><u>Example:</u> No systematic follow-up in sector ministry to audit reports → risk of no sanctioning of malpractices, of weak incentives to improve performance.</p> <p><u>Example:</u> Non-existence of internal audit → weak expenditure control, risk of un-illegible expenses, of misuse of funds.</p> <p><u>Example:</u> Only traditional budget classification; un-transparent relationship between resource allocation and priority interventions → risk of resource allocation not reflecting priorities.</p>	<p>Possible/moderate</p> <p>Likely/major</p> <p>Possible/moderate</p> <p>Likely/moderate</p>
	Partnership			
9.	Mutual observance of agreed obligations	Partnership at sector level	<p><u>Example:</u> Badly prepared annual reviews, late documentation with insufficient coverage → quality of dialogue compromised, risk of focus on wrong issues, of sub-optimal sector development.</p> <p><u>Example:</u> Weak track record in follow-up on agreed performance criteria/conditions → risk of PAF losing credibility, legitimacy of full alignment threatened.</p>	<p>Likely/moderate</p> <p>Unlikely/major</p>
10.	Consensus among all budget support donors regarding approach (incl. rules for transfer and monitoring) and conditions for general budget support	JFA if any	<p><u>Example:</u> Other donors are not willing to move from earmarked funding to budget support → Risk of loss of weight of Denmark in policy dialogue.</p>	<p>Possible/minor</p>

THE FORMULATION AND APPRAISAL PHASE

2.4. Refined risk assessment and identification of safeguards in cases of SBS

Where it was decided during the preparation to give SBS, the next step is to formulate any necessary safeguards for managing the risks.

The starting-point should be the risk assessment carried out before submission to the Programme Committee which now needs to be refined; it is on this basis that the safeguards should be defined. These should be directed towards reducing the “inherent” risks (such as the ones identified in the preliminary risk assessment) up to the point where the “residual” risks are acceptable.

Certain principles should be followed when formulating the safeguards:

- Make sure the safeguards are “non-intrusive” - meaning they should lower the risk in a way that does not substitute for national procedures and/or policies or take away responsibility from the national actors or systems. Otherwise they would violate the high level of alignment of SBS.
- Include normally medium-term safeguards, typically capacity development, to address the weaknesses and constraints identified. This generally is the most sustainable way to manage risk in relation to (Danish) programme support - i.e. working with the partner to improve the broader administrative and fiduciary environment. Such efforts may already be on-going, e.g. as part of PFM or other reform programmes. If not, new efforts may need to be agreed with the partner organization, either as part of the support or outside of it.
- Consider if short-term safeguards are needed, which may often be the case since the results of capacity development cannot be waited. Short-term safeguards can be more difficult to design so that they are non-intrusive (and the borderline between intrusive and non-intrusive measures is not clear). Even so some types of safeguards are commonly accepted as compatible with budget support. These are preferable to the alternative of providing less aligned earmarked support, but as a rule they should be considered temporary and have an exit strategy.
- Where no short-term, non-intrusive safeguard can be mobilized for a key risk, and it is not possible to wait for the medium-term improvements, the solution should be not to use SBS in the short term. If this is the case at this stage of the preparation process despite the initial decision to go for SBS, the Representation should outline the consequences of this in the programme support proposal that it submits for appraisal.
- Use Table 3 (below) to help identify possible risks and safeguards. The table shows the typical risks for SBS (which often relate to the budget support principles 3 to 8) and examples of non-intrusive safeguards, both for the short and medium term. Note: The proposed safeguards are only meant to be indicative of ways to approach the risks sketched. They should always be formulated in more specific terms in order to reflect the situation at hand. The time perspective should also be added for the medium-term safeguards: Are they expected to impact on the risk one, two, etc. years from now?

- Use the sector dialogue (usually together with other sector donors) as the privileged forum for discussing risks and risk mitigation even though seldom mentioned explicitly in the table.
- Some of the medium-term safeguards (in particular relating to PFM) cannot be addressed as part of the support to the sector or area since they depend on improvements or reforms that should cover the whole of the public sector in order to have any effect. But the sector at hand may manage to become a pilot case, thus perhaps accelerating the impact on the sector. In other instances, the sector has no influence on the timing and design of the measures to be implemented.
- Having identified possible safeguards matching the risks identified, then assess to which extent they actually reduce the risks to acceptable levels. To the extent some of the (residual) risks remain high, the Representation will emphasise this in the risk section of the programme support document and include them in the risk mitigation plan required (see GPM Part 2, section 5), including information on who is responsible for keeping them under observation and following up on them.

Table 3: Examples of risks and safeguards

GBS principle	Issue covered at sector level	Examples of risks identified	Examples of risk assessment	Examples of short-term safeguards	Examples of medium-term safeguards
3.	Sector/thematic plan/strategy/programme	<p><u>Example:</u> No proper costing of sector strategic plan → risk of compromised feasibility, of “shopping list” character, of unsatisfactory real prioritisation and outturn.</p> <p><u>Example:</u> Well-costed sector plan out of tune with expected available resources → risk of arbitrary implementation, thin spreading of resources, weak outcomes.</p> <p><u>Example:</u> No multi-year perspective, only annual work plans and budgets → risk of no link to policy and to expected longer-term outcomes.</p> <p><u>Example:</u> Over-emphasis in sector strategy on tertiary health → risk of weak poverty impact (= case of disagreement between partner country and Danida priorities)</p> <p><u>Example:</u> Little involvement of sub-national authorities in planning and management, little local ownership of sector objectives → risk of weak reflection of national priorities at local level, of weak service delivery and sector governance</p> <p><u>Example:</u> <u>Vested interest against program policies and reforms from different stakeholders</u></p>	<p>Likely/moderate</p> <p>Almost certain/major</p> <p>Likely/catastrophic</p> <p>Likely/moderate</p> <p>Possible/major</p> <p>Likely/moderate</p>	<p>Agreement on strict prioritisation and costing of annual work plan</p> <p>Same as above</p> <p>(Hardly any feasible measure → SBS to be postponed)</p> <p>Agreement on appropriate prioritisation of annual work plan and budget. Condition on sub-sector shares of budget.</p> <p>Agreement of real involvement of local authorities in annual work planning. Support to immediate seminars between national and local sector stakeholders</p> <p>Identification of key vested interested through structured stakeholder analysis. Based on this, design strategies, e.g. cooptation measures of stakeholders and/or adjust policy ambitions. Mitigating actions to be reflected in PAF</p>	<p>Support for development of reference unit costs and costing method, and for actual costing. Support for development of sector MTEF.</p> <p>Support for reformulation of plan in tune with MTEF, for strengthening of planning system, for better cooperation sector ministry/MoF (Ministry of Finance).</p> <p>Support for development of costed medium-term strategic plan.</p> <p>Dialogue on sector policy; support for studies on public health outcomes of sector policy options.</p> <p>Support for revised policy formulation and planning procedures; for participative review of sector plan and reformulation involving local stakeholders.</p> <p>Dialogue on sector policy reforms based on systematic assessment of reform commitment. Mitigating actions to be reflected in PAF</p>
4.	<p>Previous poverty reduction results in sector/area</p> <p>Monitoring system at sector level</p>	<p><u>Example:</u> Unreliable data as basis of reports → risk of misguided implementation.</p> <p><u>Example:</u> Only progress (activity) monitoring established → risk of weak and unsystematic knowledge of wider and longer-term effects</p>	<p>Possible/moderate</p>	<p>Support for one-off sample survey to verify critical data as part of annual planning and budgeting.</p> <p>Quick sample surveys of relationship between</p>	<p>Support for improved data collection, data analysis, etc.: Staff training, organisation, management, public availability, ...</p>

GBS principle	Issue covered at sector level	Examples of risks identified	Examples of risk assessment	Examples of short-term safeguards	Examples of medium-term safeguards
		<p>(outcomes), of relationship with policy.</p> <p><u>Example:</u> Much sector information exists, but is fragmented and unsystematic → risk of contradictory management information, unreliable feed-back to implementation, insufficient knowledge of outcomes.</p> <p><u>Example:</u> Sector monitoring system in place on paper, but given insufficient resources → risk of unreliable, infrequent, insufficient information on progress and outcomes.</p>	<p>Likely/major</p> <p>Likely/moderate</p> <p>Likely/major</p>	<p>activities/outputs and outcomes.</p> <p>Short-term TA to map availability of data, reach preliminary conclusion on compatibility of data sources, relative data reliability, validity of assumed knowledge, etc.</p> <p>Agreement on higher share of annual sector budget. Short-term earmarked funding might be considered in addition to SBS.</p>	<p>Support for establishment of all-round sector monitoring system, including implementation of baseline survey.</p> <p>Process to establish coherent network of information-holders, sector data system, consolidated reporting. Put peer pressure on non-aligned donors to integrate monitoring systems, make available information.</p> <p>Analysis of specified system to rationalise, optimise, minimise costs. Medium-term agreement on sufficient funding.</p>
5.	Finance Act process	<p><u>Example:</u> Min. of Finance bullies sector ministry → risk that sector priorities not well reflected in state budget.</p> <p><u>Example:</u> Sector receives insufficient or falling share of state budget (ref. international standards, achievement of MDGs, etc.) → insufficient outcomes.</p>	<p>Likely/moderate</p> <p>Possible/moderate</p>	<p>Donor (moral) support to sector ministry in forums including MoF. Insistence on MoF participation in sector reviews. Condition.</p> <p>Agreement with MoF on sector allocations. Additionality- or other resource-related condition</p>	<p>Support to sector ministry for strengthening case, garnering support and understanding from parliamentarians, pressure groups, ...</p> <p>Maintenance of condition. Analysis of sector expenditure management (e.g. Public Expenditure Review in sector) aiming at rationalisation, efficiency gains, higher value-for-money.</p>
6.	Procurement (included in principle 8)	<p><u>Example:</u> Procurement rules accord with international best practice but weak compliance → risk of corruption, of low value for money.</p> <p><u>Example:</u> Procurement process very slow → risk of slow budget execution, low achievement of objectives.</p>	<p>Possible/moderate</p> <p>Almost certain/moderate</p>	<p>Agreement on (donor-funded) procurement audits.</p> <p>Specialised TA in procurement committee.</p> <p>Support for (improved) annual and medium-term procurement planning</p>	<p>Support for reorganisation of procurement function, for internal and external controls of compliance, for competence development, ... (Note: Only partly within sector responsibility)</p> <p>Analysis of procurement process, of bottlenecks, constraints. Revision of procedures, staff training, institutionalised procurement audits. Introduction of performance budgeting. (Note: Only partly within sector responsibility)</p>
7.	Supreme audit	<p><u>Example:</u> Lacking independence of the Supreme Audit Institution (SAI) → difficult to hold key players in the sector accountable, risk of weak incentives to</p>	<p>Possible/major</p>	<p>Agreement on external value-for-money studies, expenditure tracking exercises, procurement</p>	<p>Work to get supreme audit-set-up reformed. Fall-back: Work to improve or introduce other controls external to the sector (state</p>

GBS principle	Issue covered at sector level	Examples of risks identified	Examples of risk assessment	Examples of short-term safeguards	Examples of medium-term safeguards
		strengthen financial controls and general compliance with regulations, risk of continued inefficiency, loss of funds, etc. <u>Example:</u> SAI has low capacity; irregular audit of sector institutions → risk of impunity, of deterioration of compliance, of increasing fiduciary risks.	Likely/major	audits. Same as above	inspectorate, etc.) and to improve internal controls and performance reviews (value-for-money, procurement, expenditure tracking). (Note: Only partly within sector responsibility) Support capacity development of SAI. Work for increased budget allocations. Support internal controls and performance reviews. (Note: Only partly within sector responsibility)
8.	Quality of PFM at sector/thematic level (other issues than under 5 – 7)	<u>Example:</u> Only traditional budget classification; un-transparent relationship between resource allocation and priority interventions → risk of resource allocation not reflecting priorities. <u>Example:</u> Unreliable and irregular in-year budget execution reports → actual level of expenditure not well known before end-year, risk of over- or under-expenditure, risk of skewed expenditure across sector. <u>Example:</u> Non-existence of internal audit → weak expenditure control, risk of un-illegible expenses, of misuse of funds. <u>Example:</u> No systematic follow-up in sector ministry to audit reports → risk of no sanctioning of malpractices, of weak incentives to improve performance.	Unlikely/moderate Likely/moderate Possible/moderate Likely/major	Close monitoring of progress of activities, of production of outputs Agreement on acute beefing-up of capacity to improve Strengthening of other internal compliance controls; sample controls Pressure; condition relating to follow-up	Introduction of output-based budgeting/programme budgeting as part of PFM reform (work to have sector selected as pilot) Establishment of integrated financial management information system (IFMIS) as part of PFM reform Introduction of internal audit in national PFM systems as part of PFM reform Work to strengthen domestic demands (in particular Parliament) for follow-up, for accountability. Work to strengthen power and status of SAI.

2.5. Identification of maximum level of alignment in cases where SBS is not chosen

For programmes or components where SBS has been assessed not to be possible, the Danish funds will necessarily be earmarked for specific uses.

This can be for the Danish funds separately or as part of a joint funding arrangement (basket fund). The earmarking can also be narrow or broad - ranging from a few select activities to the bulk of the sector's or area's expenditure (e.g. all expenditure except salaries) - and it can make use of the country's or partner's systems to very different degrees; the support can be given based on procedures that are totally parallel and different from the partner's, or it can use of most of the partner's rules and procedures (but keeping the funds earmarked).

There can be several reasons for choosing to earmark support:

- The nature of the targeted activities (e.g. piloting of innovative activities)
- Ensuring the funding of activities that are likely to receive too little attention by the partner through the ordinary budget
- Lacking preconditions for SBS (such as a lack of a partner programme to support) or unacceptable risks associated with SBS.

Regardless of the reason, the funds should be given in the best-aligned way possible.

When considering to earmark funds to support a programme consider the following points and steps:

- Consider carefully the alternative risks of earmarking since non-partner financial and procurement regulations are not necessarily more efficient or less prone to risk. Parallel procedures and structures may be set up because the risks of SBS are seen to be too high - but there can be significant administrative challenges which lead to new risks (e.g. incentives for abuse) of setting up parallel procedures, especially where large funds are involved. New lines of accountability and patronage are created, which are possibly less well understood. Also, parallel procedures may undermine or delay longer-term systemic improvements, attract skilled staff away from essential functions, and create an over-reliance on external TA.
- Seek local expertise to help in optimizing the level of alignment, in particular regarding the central aspects of the country systems, namely the planning framework, the monitoring system, and the PFM system (cf. budget support principles 3 to 8). Identifying the maximal level of alignment requires in-depth knowledge of the country systems, and superficial knowledge of them has in many cases led to choosing low-alignment solutions or to remaining more or less automatically at the level already practiced (or practiced by other donors).
- Recognise that there are several different dimensions of alignment which may not depend on each other - and differentiate the alignment level according to needs if relevant: If the major constraint is lack of a well-developed partner programme, this

does not mean that a government's PFM system and procedures cannot be used; If the constraint is lack of a monitoring system, a well-functioning PFM system can still be used. Conversely, if the PFM system is the main worry while the sector's strategic plan is consistent and feasible (and progress reporting is ok), then it makes sense to allow the Danish support to be spent against all of the planned activities even if earmarking them, i.e. making them traceable.

- Differentiate the level of alignment also within the PFM system itself based on where the main risks are identified. Refer to table 4 for guidance to do this.⁶ But recognise that PFM systems are different in many respects, which means the comments in the table are only indicative. Recognise also that each of the dimensions is composite on its own, and alignment with smaller or bigger modifications is often possible with respect to each. For instance: If there is limited capacity of the SAI, partial use of the national audit system can be necessary. If the ordinary reports are sub-standard or late, use the accounting system partially only by requesting special financial reports. If the budgets lack a programme or output dimension, then try to temporarily mitigate this by using a spreadsheet that links the ordinary classification and the desired supplementary one and use it to budget and to report on programme expenditure in parallel with the official system. Consider only these measures in contexts where PFM reforms are already about to address the bottlenecks in question, and usually in collaboration with other donors as part of a joint effort to speed up alignment.

⁶ See also the SPA/CAPRI report on "Putting aid on budget" [[link](#)].

Table 4: Dimensions of “on budget”

	Explanation	Comments; Danish minimum requirements
On Plan	Aid spending is integrated into spending agencies’ strategic planning and supporting documentation for policy intentions behind the budget submissions.	<p>All Danish support to the public sector should be “on plan”, regardless of whether it is aligned along the other dimensions.</p> <p>This requires projected medium-term disbursement figures and targeted objectives/priorities to be known to sector ministry in time for inclusion in sector financing plan and sector MTEF.</p>
On Budget	External financing and its intended use are reported in the budget documentation.	<p>All Danish support to the public sector must be “on budget” in this narrow sense, regardless of whether it is aligned along the other dimensions.</p> <p>This requires the programme budgets to be structured in a way that allows them to be clearly and easily reflected in the national budget classification and that the deadline for informing MoF and/or sector ministry of next year’s disbursements is respected.</p>
On Parliament (or “through budget”)	External financing is included in the revenue and appropriations approved by parliament.	<p>In most countries, in its strict sense this only applies to GBS and usually SBS. Parliament is informed about, but usually does not approve earmarked funding, and only if the funds are reflected in the budget documents, i.e. are “on budget” in the sense of the row above.</p> <p>In principle, all Danish support to the public sector will automatically be “on parliament” in the sense that follows from its being “on budget”.</p> <p>Support being on budget and on parliament is not necessarily on treasury, on accounting, etc. E.g. it may be disbursed directly to sector institutions (but normally should not !)</p>
On Treasury	External financing is disbursed into the main revenue funds of government and managed through government’s systems.	<p>In most countries, both un-earmarked (i.e. budget) support and earmarked support can be handled by the official payment system if disbursed to the treasury.</p> <p>On treasury and on accounting usually go together (e.g. due to legislation in some countries: Only expenditure against funds disbursed through the official payment system can be accounted for in the official accounting system). But in some countries, support not on treasury may be on accounting.</p>
On Accounting	External financing is recorded and accounted for in government’s accounting system, in line with government’s classification system.	<p>Note that aid is not fully on accounting as long as additional financial reports are required.</p> <p>Aid on accounting is also in principle on audit.</p>

	Explanation	Comments; Danish minimum requirements
On Audit	External financing is audited by government's auditing system.	Aid not on accounting could be put on audit by special arrangement. Budget support is on audit by definition. For earmarked support, the SAI should if possible be involved in the contracting of private auditing companies, if the SAI itself cannot carry out the audits.
On Procurement	Procurement done according to national procurement procedures	Internationally accepted standards

Source: Dimensions and explanations from CAPRI/SPA report.

This also goes for the funding of temporary additional capacity as suggested by some donors, e.g. of external accountants to prop up capacity and quality of the accounting (reconciliations, reporting, etc.) or of extra staff to perform processing and controls of payments in the treasury.

It should finally be noted that alignment in the planning and budget dimensions does not in itself imply any fiduciary risks but merely require the donor to manage the programme support in a timely fashion, responsive to the planning and budgeting cycle of the partner.

2.6. Organisational capacity assessment

The GPM require that the capacity of the partner organisations is assessed during the programme support formulation. The overall purposes can be i) to help identify which modality to use (including SBS) and how to design the support or ii) how to support the development of the capacity of the partner organisations' during implementation (regardless of modality). These purposes can be further broken down into the following:

- enable the Danida to decide on the design, scope, and size of the support to a sector programme (or to individual organisations within the programme) so that it is commensurate with the implementation capacity in the sector;
- target technical assistance to the actual needs of the organisation
- enable partner authorities to design and prepare a capacity development plan;
- enable partners and development partners to decide on the scope and modalities for support to capacity development;
- create awareness among staff members and stakeholders about possible need for change;
- inform the policy dialogue between sector partners.

The specific purpose of the capacity assessment has important consequences for its scope and the best way to approach it.

Consider the following pointers when planning and implementing a capacity assessment of the sector, area or individual organisations⁷.

- Clarify the purpose or aim of the capacity assessment (consider the options above) and define the focus and content of the assessment based on its purpose: Is the focus on the sector as a whole (which implies a broader institutional focus) or on individual organisations (a more confined organisational focus)?
- Consider any existing studies or capacity assessments already undertaken of the sector or target organisations, and assess the need for further assessment, if any.
- If further capacity assessment is needed, clarify its scope. Where SBS has been chosen, the capacity assessment will in principle cover the sector/subsector/thematic area. Where the support will be earmarked, the assessment will usually cover the organisations that will be supported. Make every effort to make the assessment a joint-effort between the active donors in the sector and the target institutions.
- Use the TOR in the appendix of the *Toolkit for Capacity Development in a Sector Context* 2009 [[link](#)] which provides guidance for both situations⁸.
- Decide on the overall approach based on the purpose of the capacity assessment. If the aim is to support future change and capacity assessment, then a very participatory and more comprehensive approach is needed which also includes identification of change management issues. If the purpose is to help the donor decide about how and how much to support capacity development, then a more desk-based and selective approach may be best in order to avoid high transaction costs and that false expectations or anxiety are created in the target organizations.
- Clearly define who is the owner or responsible authority of the capacity assessment. Unclear roles can easily undermine effective accountability, legitimacy and transparency of the assessment. If no one is acting as the lead, there is a risk that no one will eventually feel committed to acting on the results of the assessment. Therefore clearly state whether the assessment is made by Danida and other development partners to enable their internal decision-making, by the sector authorities, by the management and/or boards of particular sector organizations, or by several or all of these stakeholders, in which case it is crucial to indicate the primary owner of the assessment.
- Clarify the need for external consultants and what roles they will play. External consultants can be helpful in conducting the assessment and do the practical work of creating spaces for exchanges, collecting data, assembling viewpoints, suggesting interpretations and preparing analysis. But external consultants cannot “own” the assessment process.
- For assessments aimed at preparing the ground for capacity development support in the target organisations, define a broad range of outputs of the capacity assessment to make sure that it gets the largest possible impact. Its result should be much more than

⁷ See Boesen and Therkildsen (2004): Capacity Development Evaluation – between Naivety and Cynicism

⁸ See “Guidance note on Danish support for capacity development” and European Commission 2009. Aid delivery methods programme. Checklist for capacity development support. European Commission, Brussels.

just a report. Several other (and more important) tangible as well as process-type outputs should be considered and specified, such as:

- a final workshop for core group/key stakeholders;
 - orientation event(s) for external stakeholders;
 - a debriefing event for senior executives;
 - debriefing event(s) for staff members;
 - a summary two-page overview in easily accessible form for wider circulation;
 - confidential papers/reports on special issues;
 - draft reports circulated as specified;
 - a final report;
 - compact disk (CD-ROM) versions of final reports and appendixes; and
 - web posting and/or publication of final reports, etc.
- Use the TOR for a capacity assessment presented in the Appendix for inspiration when designing the assessment. Consult also the "[Guidance note on Danish support for capacity development](#)" and in "[Guidelines for use of technical assistance](#)" available at [AMG](#), as well as "[A Results-Oriented Approach to Capacity Change \(ROACH\)](#)", also available at [AMG](#).

Box 3: Capacity assessments - typical elements

The typical themes in a capacity assessment include

- *the organizations* to be included, as appropriate, explaining why they are key to the success of envisaged or ongoing support to the sector;
- *data collection* about past and present outputs, their relevance, quality, and quantity (services, products, and regulations) from the sector/subsector/specific organizations included in the CA (Capacity Assessment). If the assessment is also an input to consideration of future CD (capacity development) activities and CD support, then this baseline information is essential when a CD action plan will identify and specify desired future outputs, because they have to be realistically projected.
- *the sector context*, including structural factors relevant to capacity (e.g., extended territory and limited public resources are likely to have an impact on the ability to fund and deliver items such as health and education services territory-wide), institutional and political economy factors (including, but not limited to, the legal framework and how this is observed and enforced; public-sector-wide factors related to civil service conditions, etc.; decentralization; patronage/client systems affecting the public sector's performance; and effectiveness and modalities of sector governance and accountability mechanisms);
- *drivers and constraints*, which are especially difficult but important to assess, but explain present performance and may explain why capacity may not grow easily;
- *inputs and resources available* to the sector and the organizations, including the balance between funds for different purposes and the past trends in areas such as spending on maintenance, operational costs, salaries, and staff numbers;
- *the internal elements* of the organizations under assessment (leadership, strategy, structures, rewards and incentives, internal relationships, and helpful mechanisms - several good ways of decomposing the internal capacity are available, and the choice may best be left to those performing the assessment and/or the organizations under assessment); and
- *the sector networks and external networks* and relations, including the sector governance set-up.

Appendix: Some conceptual guidance regarding risks and risk management

a. Risk terminology

The following is the terminology often used in risk assessments.

Table: Risk Terminology

Risk	Uncertainty of outcome is the combination of likelihood and impact, including perceived importance.
Exposure	The consequences, as a combination of impact and likelihood, which may be experienced by Danida if a specific risk is realized
Inherent risk	The exposure arising from a specific risk before any action has been taken to manage it.
Residual risk	The exposure arising from a specific risk after [effective] action has been taken to manage it.
Risk acceptance	The informed decision to accept the consequences (impact) and the likelihood of a particular risk.
Risk appetite	The amount of risk that an organisation is prepared to accept, tolerate, or be exposed to at any point in time.
Risk avoidance	An informed decision not to become involved in a risk situation
Risk management	All the processes involved in identifying, assessing and judging risks, assigning ownership, taking actions to mitigate or anticipate them, and monitoring and reviewing progress.
Risk mitigation	The processes built into the controls environment, such as policies, frameworks, accountabilities etc to lower the residual risk.
Intrusive safeguard	A measure to lower the inherent risk by directly interfering with national procedures or policies.
Non-Intrusive safeguard	A measure to lower the inherent risk in a way which does not substitute for national procedures and / or policies, or draws away responsibility from these.

Source: Adapted from Lister et al., 2008

b. Types of risk

Risks can be categorised in various ways of which the table below represents just one. By clearly cataloguing risks it becomes easier to assess and address them in a concise and constructive way. Still, it is important not to lose sight of the overlaps, and the interactions, between the different categories of risk: Fiduciary risks are in fact one type of governance

risks, and the risk of corruption may be behind a number of other risks, just as the quality of democracy may be behind weaknesses in planning, implementation of plans (including monitoring), PFM, etc.

A type of risk not included below is “reputational risk”. This is the risk incurred by the donor organisation of losing part of its good reputation (among the politicians, opinion leaders, and/or the tax-payers at home) by being linked with undesirable or unacceptable incidents in the supported countries or sectors (such as corruption scandals, breaches of human rights, etc.). This risk is generally considered to be higher in the case of budget support than of earmarked support due to the un-earmarked nature of budget support.

In the final analysis, all categories of risks should be seen in light of their possible impact on achieving the intended development impact of the support.

Table: Risk Categories

Risks		Definition: Risk that...	Budget Support Principle
1. Fiduciary risks		<ul style="list-style-type: none"> - funds are not used for the intended purposes - funds are not properly accounted for - funds do not achieve value for money 	# 5, 6, 7, 8
2. Non-financial risks	Governance risks	<ul style="list-style-type: none"> - the achievement of poverty reduction objectives is compromised by weak governance in terms of <ul style="list-style-type: none"> - democracy, rule of law, human rights, etc. - policies, plans and the will to implement them - partnership with non-government stakeholders - etc. 	# 1, 2, 3, 4, 9, 10
	Macroeconomic risks	<ul style="list-style-type: none"> - the achievement of poverty reduction objectives is compromised by the macroeconomic framework 	Not covered by the ten principles, but should be part of the overall risk assessment

c. Assessment of risks

The following principles apply when analyzing and assessing risks:

- (i) Performance & Progress: Account should be taken of both actual performance, the trend of progress, and already on-going or planned measures relating to the issue identified as a risk.
- (ii) Absolute risk: The risk assessment should be made on an absolute rather than a relative basis, i.e. focusing on the level of risk arising from the systems of the country in question, not how well or poorly its systems compare to those in other countries.
- (iii) Inclusive: The assessment of the risks should as far as possible be shared by the partner and other donors, since the needed safeguards must be thought through and formulated in collaboration with them in order to avoid fragmentation and inefficiency.

Impact and likelihood: As mentioned in the section above, risks are assessed along two dimensions: Impact and likelihood. The matrix below, with the impact indicated on a scale of "insignificant / minor / moderate/ major/ catastrophic" and the likelihood on a scale of "rare / unlikely / possible / likely / almost certain", is meant to illustrate this: In general terms, the combination of expected impact and likelihood of risk occurrence will give an indication of whether a risk is acceptable, unacceptable, or whether it falls in between for concrete management resolution by the Representation. Circumstances being different and risks being of varying importance, the table is however not meant as a key substituting for concrete decision-making in each case.

Figure: Assessing the Risks

Likelihood	Almost certain	Acceptable	?	Unacceptable	Unacceptable	Unacceptable
	Likely	Acceptable	?	?	Unacceptable	Unacceptable
	Possible	Acceptable	Acceptable	?	?	Unacceptable
	Unlikely	Acceptable	Acceptable	Acceptable	?	?
	Rare	Acceptable	Acceptable	Acceptable	Acceptable	Acceptable
		<i>Insignificant</i>	<i>Minor</i>	<i>Moderate</i>	<i>Major</i>	<i>Catastrophic</i>
						Impact

Links

Guidelines on the provision of Budget Support at the AMG-site:
<http://amg.um.dk/en/menu/TechnicalGuidelines/BudgetSupport/>

The PEFA assessment tool: http://www.pefa.org/pfm_performance_frameworkmn.php

Link to PFM-Study of the health sector of Mozambique in 2009:
<http://www.danidadevforum.um.dk/en/menu/Topics/GoodGovernance/PublicSectorManagement/PublicFinancialManagement/PublicFinancialManagement.htm?WBCMODE=PresentationUnpublished>

Link to "Putting Aid on Budget. A Study for the Collaborative Africa Budget Reform Initiative (CABRI) and the Strategic Partnership with Africa (SPA): <http://www.mokoro.co.uk/aob.htm>

The Danish public sector management strategy ("Effective and Accountable Public-Sector Management. Strategic Priorities"):
<http://amg.um.dk/en/menu/PoliciesAndStrategies/GoodGovernance/PublicSectorManagement/>

The World Bank PSIA (Poverty and Social Impact Analysis) Source Book: <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTPOVERTY/EXTPSIA/0,,menuPK:490139~pagePK:149018~piPK:149093~theSitePK:490130,00.html>

"Stakeholder Power Analysis" of the International Institute for Environment and Development (IIED): <http://www.policy-powertools.org/Tools/Understanding/SPA.html>

Tools and Methods Series, European Commission, 2009 and EuropeAid's "Toolkit for Capacity Development in a sector context":
<http://capacity4dev.ec.europa.eu/topic/2025/taxonomy/term/2354>

PEFA website: <http://www.pefa.org/index.php>

Danida Development Forum - Monitoring and Indicators
<http://www.danidadevforum.um.dk/en/menu/MonitoringAndIndicators/>

"Guidance note on Danish support for capacity development":
<http://amg.um.dk/en/menu/TechnicalGuidelines/Capacity+Development/>

"Guidelines for use of technical assistance":
<http://amg.um.dk/en/menu/TechnicalGuidelines/TechnicalAssistance/TechnicalAssistance.htm>

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<http://www.um.dk/NR/rdonlyres/780914AD-A4C4-42C2-8039-8115F4CA0DDB/0/KortCD-briefintro.pdf>

The World Bank PSIA (Poverty and Social Impact Analysis) Source Book:
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Ministry of Foreign Affairs of Denmark

Asiatisk Plads 2
DK-1448 Copenhagen K
Denmark

Phone: +45 33 92 00 00

Fax: +45 32 54 05 33

Email: um@um.dk

Internet: www.um.dk

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