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FISCAL AND FINANCIAL MANAGEMENT IN AFGHANISTAN

PRESENT CONDITIONS AND OPTIONS FOR REFORM AND
ASSISTANCE: A SUB-NATIONAL PERSPECTIVE

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I.0 INTRODUCTION

I.1 OVERVIEW

After more than twenty years of war and administrative chaos the Government of Afghanistan (GoA) is trying to regain its citizens' confidence in democratic institutions to solve their conflicts and to attend to their basic needs. In parallel with political, fiscal and administrative reforms pursued in recent years, the GoA has sought to expand, solidify and legitimize its presence outside Kabul. The enhanced central government presence at provincial and district levels has multiple goals and dimensions, including stabilization and security, but also implies a capacity to improve the delivery of public goods and services, and ability to reach previously. The reassertion of central government presence and of the rule of law at sub-national levels and improvement in the provision of public services are broadly viewed as pre-requisites for rebuilding working alliances between the state and sub-national constituencies.

Well-established local governments and effective inter-governmental fiscal relations are known to be the optimal types of institutional arrangements for attending to local demands. The dual role of local communities as consumers of public goods and services and as taxpayers to finance them provides a sound framework for their effective and efficient delivery. The beneficiary's closeness to administration and local authorities allows for more participation and accountability.

Public Financial Management (PFM) comprises a set of institutions that dictates the way public resources ought to be managed to attend to public demands. PFM combines - norms, procedures and existing practices- employed to plan, formulate, approve, execute and control public resources. These institutions and how they work finally help to shape fiscal outcomes, especially in the delivery of social services. An operative public financial management system is at the basis of well funded sub-national administrations, hence the increasing attention giving by the GoA to these two and to their capability to carry out its overall strategy.

At this time in Afghanistan there are neither well established or autonomous local governments nor well functioning PFMs. Political and cultural tradition never allowed for the former; and under present conditions scarce resources are primarily devoted to rebuilding an operative central government which would be able to answer for the most pressing needs of its citizens. This is not to say the GoA is doing nothing in the above-mentioned fronts. On the contrary, as it will be shown later, budget programming and implementation has improved, especially on attention to timely salary payments. Also there is an appreciable administrative and organizational movement to improve the capacity of public organizations and civil servants' efficiency at a sub-national level.

This report reviews existing financial management procedures within the GoA, particularly at the sub-national level, and provides options for better resource management, having in mind the need to improve the provision of public goods and services. It also seeks to identify those qualities and factors –knowledge, skills, attitude and working conditions- that affect performance and provide guidelines for technical assistance and training to improve the effectiveness of staff and organizations in managing public resources. This assistance is also expected to provide elements to improve financial management procedures and practices of Afghanistan Stabilization Program (ASP) which is a key instrument in the Government's strategy.

Initial attention was given to understand the institutional framework for financial management in Afghanistan. It was accomplished by examining legal and normative documents as well as by interviewing high ranking officials in the Ministry of Finance (MoF) and in other central government entities. These elements permitted mapping the procedures and practices employed to manage public resources and the interactions with sub-national entities. Several field trips helped to evaluate formal procedures as established in norms against existing practices in the operative agencies. The sample of provinces and districts, though

geographically skewed for security reasons, covers their three grades classification. Most of the recommendations presented in this report were elaborated by consultation with officials from respective entities; nonetheless all of them require further elaboration and discussion with responsible authorities.

Initially the report presents some definitions and conceptual elements related to financial management issues. This is followed by a brief examination of fiscal conditions in Afghanistan and constraints and possibilities as well as ongoing government reforms to improve financial and administrative management. Later, the report provides an evaluation of financial management practices and the role played by sub-national entities. The fourth chapter presents some recommendations to improve financial management and provides some options to consolidate government reforms. Here, there are also some guidelines for TA&T to enhance capabilities of government officials, especially from sub-national governments. The final chapter presents an initial evaluation of financial management in three cities: Kabul, Herat and Mazar-i-Sharif; it also includes some critical elements to design a program to improve their fiscal and financial management.

Finally, the report presents a summary with 10 programs and projects to help improving Fiscal and Financial Management in Afghanistan. Five of the most important projects are included in the Action Plan to be carried on by the Afghanistan Local Governance Assistance Project (ALGAP).

I.2 PUBLIC FINANCIAL MANAGEMENT IN AFGHANISTAN: THEORY AND PRACTICE

To attend the basic needs of its population, a Government collects taxes and assigns, manages and controls those resources; in this manner they assemble the budget for a given fiscal year. Public Financial Management refers to all budget processes: planning, programming, approval, execution, accounting, reporting, monitoring and evaluation and control of public resources and to the institutional arrangement –legal and informal norms and procedures- that govern their performance. In a broader way it also includes the use of financial instruments such as medium term expenditure frameworks, cash management and norms and guidelines for procuring goods and services. In addition, organizations and their management capacity are fundamental to understand and evaluate public financial management.

The three broad objectives for public financial management are: fiscal discipline for macroeconomic stability, allocation of resources to strategic priorities and managerial efficiency in delivering public goods and services. That is, in an effective financial management arrangement, total expenditures should be closely aligned to what is affordable; spending should be allocated to match policy priorities and the provision of public goods and services should be cost effective.

These are not to be independent objectives. In many cases the pursuit of fiscal discipline is often achieved by reordering or cutting down priorities and damaging service delivery. Similarly, a lack of budgetary realism leads to a mismatch between promises, resources and outcomes, ending up in growing mistrust and lack of confidence in governments. Well coordinated interdependence among these three objectives should create an enabling environment for development purposes where fiscal discipline incentives better allocation and more effective and efficient use of resources.

Fiduciary risk, defined as the possibility that actual expenditures differ from authorized expenditures or that public funds may be misused or even stolen, is a leading criterion for assessing performance of financial management systems. This is quite an important issue for the multilateral entities and donors who provide those resources though it is no less important for governments under resource constraints and an urgent need to deliver results. This assessment focuses on the possibilities of sub-national administrations to introduce greater efficiency and effectiveness in the management of public resources, the so-called development side of financial management.

Traditionally, public financial management assessments stop at fiscal discipline issues focusing thereby in the institutional elements that may promote or allow fiduciary risk. These types of assessments put aside the other two objectives and deduce from the fiscal constraint the whereabouts of local and regional governments as well as the incentives and performance of public enterprises. This is a customary approach especially for assessing central government financial management in unitary states. In these regimes decision making follows a top-down process and sub-national entities are merely budget operators carrying on explicitly delegated functions and therefore not able to affect fiscal aggregates.

Presently, Afghanistan closely follows the unitary model with a highly centralized political, fiscal and administrative organization. The central government has legal responsibility for the provision of basic goods and services including education, health, defense, policing, etc. Municipalities form a different level of government, with explicit responsibilities established by the law¹. They own tax revenues and have relative budget autonomy. Provinces and districts are legally recognized as Local Administrative Units and have over sixty responsibilities clearly established for the Province and District Governors. However under the present legal and administrative scheme, they do not have budget autonomy or resources beyond making operative changes in the Governor's own budget.

Under this government scheme, all revenues, with the exemption of those assigned to municipalities, belong to the central government. Until fiscal year 1383, the corresponding line ministry would assign a quarterly allotment for each province which could be changed without consulting the provincial entity. This year (1384), the budget includes annual allotments for sectors and by provinces which can only - be changed with a well-founded petition by the minister to the MoF. Though by no means a provincial budget, provincial governors have no authority to manage those resources. This change in budgeting rules and other political and administrative reforms, show a blurred yet steady path towards a delegation of some responsibilities to sub-national units.

Further actions in this direction demands an assessment that goes beyond pure fiscal issues and focuses rather on the role of sub-national units in the provision of public goods and services. Growing expectations on this regard make it unavoidable to consider the effective and potential contribution of these administrations even if they are not legally responsible for the budget outcomes. Sub-national administrations are the first contact point between common citizens and the state whereby people will build their confidence according to this initial experience.

Further considerations in terms of territorial inequalities in access to basic needs and considerable administrative differential among provinces and districts support the need to explicitly consider the role of these units in the financial management process. According to a study done by the World Bank (2004 a) ill equipped, poorly paid, and ineffective provincial and district administration undermines confidence in central government thereby contributing to their resistance to the encroachment of a central authority. This issue has become even more critical since the fiscal year 1383 with the transfer to the central treasury of all revenues collected by Mustufiats (Provinces) and the uneven response given by the central government until now.

By any measure Afghanistan is one of the poorest countries in the world. Economic and social indicators: per capita GDP (including the opium economy) of us\$350, school enrollment rate 54%, under-five mortality rate 172 per 1,000 live births, and infant mortality rate 115 per 1,000 live births are among the worst in the world². These indicators become even more dramatic when considering them at the provincial level. Level of coverage of social services in poor provinces (grade 3) easily drops to a third of the coverage in provinces grade 1. Though pre-conflict Afghanistan was already lagging in quality and coverage of basic public needs,

¹ Law of Municipalities. 16 Jadi, 1336.

² Afghanistan. State Building , Sustained Growth and Reducing Poverty. A country Economic Report. September 9, 2004. Document of the World Bank.

the collapse of public service delivery occurred during the years of conflict helps to explain the present conditions but also signals a point of entry for its reversal.

Two other components not contemplated in traditional public financial management assessments deserve attention. The first one considers the effects upon the provision of local public goods induced by present fiscal conditions in Afghanistan and the need to consider the possibility to increase tax collection at the provincial level. Traditional analysis concentrates on downstream procedures to assign, manage and control expenditures leaving aside revenue considerations. In the case of Afghanistan, increasing overall tax revenues is a survival issue. Increasing provincial tax collection is a highly sensitive matter. Until recently the most important provinces collected and expended national revenues. The centralization of those revenues obviously reduced their level of expenditures. Any further increase in revenues must pay attention to this issue or at least it should be made more palatable to locals. This could be done through a sharing formula at the margin or a similar alternative that allows for some of the revenues to stay in the province.

Secondly, though not contemplated initially, this report includes a short review of financial management in three provincial municipalities. It also includes a brief perspective of their role in the provision of social needs. Municipalities are legally chartered entities with well established administrative structures, and duties (responsibilities) discriminated according to their revenue level and covering from the provision of water and sanitation systems, housing, roads and traffic regulation, up to price controls and birth, marriage and death recording (Law of Municipalities, articles 9 and 10). Municipalities have their own source of income, charge fees for public services and receive a share on national taxes collected in the city. Municipalities have well established procedures to formulate, approve and execute the budget which is to be controlled by the elected council. They are fiscally neutral, most provincial municipalities produce net fiscal surplus.

What follows is an enlarged public financial management assessment that includes the expected and effective role played by sub-national administration in formulating, assigning, executing, monitoring and evaluating public resources. It looks for the impact of budget procedures on fiscal stability, strategic prioritization and allocation of resources and efficiency in service delivery. Finally, the assessment provides an explanation for the “gap” between expected and observed results; and proposes institutional and organizational adjustments as well as TA&T to help improve staff and organizations’ performance.

2.0 PRESENT FISCAL CONSTRAINTS AND GOVERNMENT EFFORTS TO IMPROVE FINANCIAL AND ADMINISTRATIVE MANAGEMENT

The budget prepared each year is a reflection of societal demands translated into the expenditures allowed for by available resources collected from taxes. As a political document that establishes what and how goods are going to be provided, who is going to receive them and who is going to pay for them, the budget is beset by numerous constraints that emerge on account of three main factors:

- The political nature of the decision making process where many competing objectives reach for limited resources provoking all sorts of trade offs between them and leaving some of those issues unsolved.
- The limited amount of affordable resources defined by the size and structure of the economy as well as by the willingness of the owners to depart from those resources in the face of a blurred understanding of government purposes.
- The capability -both technical and administrative- of the State apparatus to extract the “needed” resources and to effectively apply them to the provision of public goods and services.

Afghanistan is emerging from over two decades of conflict that exerted a huge social and economic toll on its population. During this period public servants saw their working and living conditions rapidly deteriorating and finally affecting their capabilities and on-the-job performance. Meanwhile, public infrastructure was either destroyed or abandoned. Provision of public goods and services decreased dramatically as social indicators show.- In recent years Afghani people, with the help of the international community, have been mobilizing resources to rebuild a credible government that attends to the basic needs of the population as well as an economy that provides opportunities to earn a legal and adequate income. Though international resources will keep flowing in for years to come, though at a decreasing rate, there is a basic understanding that when the time comes, Afghanistan will be ready to stand on its own.

The following is a brief reference towards what this fiscally constrained environment means for present government and its efforts to improve the provision of public goods and services and the expected role for sub-national administrations within this framework. It also includes a short review of ongoing government efforts for establishing a more efficient and better performing public administration.

2.1 PRESENT FISCAL CONDITIONS AND PROSPECTIVE IN AFGHANISTAN.

There is a consensus among the Government of Afghanistan and development partners that the creation of a stable state is the cornerstone for building an enabling environment for bettering living conditions and for making a more equitable society in Afghanistan. WB (2004b). In this regard the document “*Securing Afghanistan’s Future: Accomplishment and the Strategic Path Forward (SAF)*”, establishes the following requirements: i) a well structured and functioning security sector, ii) a small public administration focused on core functions, and iii) an affordable and sustainable multi-year budget.

Afghanistan has been making substantive efforts to have a fiscally sustainable budget that covers the wage bill with its own resources by 2008/09 as was stated in the SAF. The portion of the current budget financed with its own resources has grown from 38% for the FY 1381 to 50% in FY 1384 keeping in line within the acquired commitments. During the period 1381-83 national revenues doubled showing a net increase of 1.5 % in terms of GDP. For this FY 1384 the government is proposing a growth in revenues of 30% which is a demanding goal by any standard (See table 1).

Item	1381	1382	1383	1384
Expenditures				
-Current Budget	349	429	579	678
-Uses:	132	233	259	400
-Salary.	209	196	320	278
-Non-salary.	542	208	4,524	333
-Sources:	891	257	5,103	345
-Own revenues.		1,955		1,872
-Donors.		2,384		3,180
-Development Budget.				5,052
-Uses:				5,730
- MoF.				
-Donors.				
-Source. Donors.				
Total				
Revenues (in percent of non-opium GDP)		3.2	4.5	4.8
Current expenditures (in percent of non-opium GDP)		8.5	9.8	10.5
				5.0
				10.4

Unfortunately, the growth in tax revenues is not enough. According to the table 1 the operative budget is growing faster in absolute value than the own disposable resources. In FY1381 the portion of the operative budget financed by donors was us \$209 million, but nowadays this portion is closer to us \$ 350 million. Paradoxically, the volume of international aid, us \$ 5052 million, is exerting an overwhelming pressure over the current budget while the tax administration is slowly recovering but unable to keep the pace with the current budget. Total tax revenues as percentage of GDP, 5.0% in FY 1384, are still quite below national revenues collected 30 years ago, 10.4 % of GDP.

Under present conditions where government receives pressing demands from all over one would expect a tight and revenue driven fiscal policy which asks for proven efficient management of any new expenditure proposal. In this regard the proposal advanced for the ALGAP looks to preserve fiscal balance and to enhance knowledge and managerial efficiency of public servants and organizations thereby enhancing the provision of public goods and services.

2.2 GOVERNMENT'S EFFORTS TO IMPROVE CAPABILITIES AND PERFORMANCE OF SUB-NATIONAL ENTITIES

According to the law the Independent Administrative Reform and Civil Service Commission (IARTCSC) is formally responsible for developing and overseeing merit-based recruitment procedures and civil service personnel policies and practices as well as for the coordination and management of the Public Administration Reform Program. On July 10, 2003, the GoA created the Priority Reform and Restructuring Program (PRR) for reforming and modernizing the most critical functions of the government. This instrument allows for

some staff to be given higher salaries for fixed terms; it also permits streamlining organizations and functional structures.

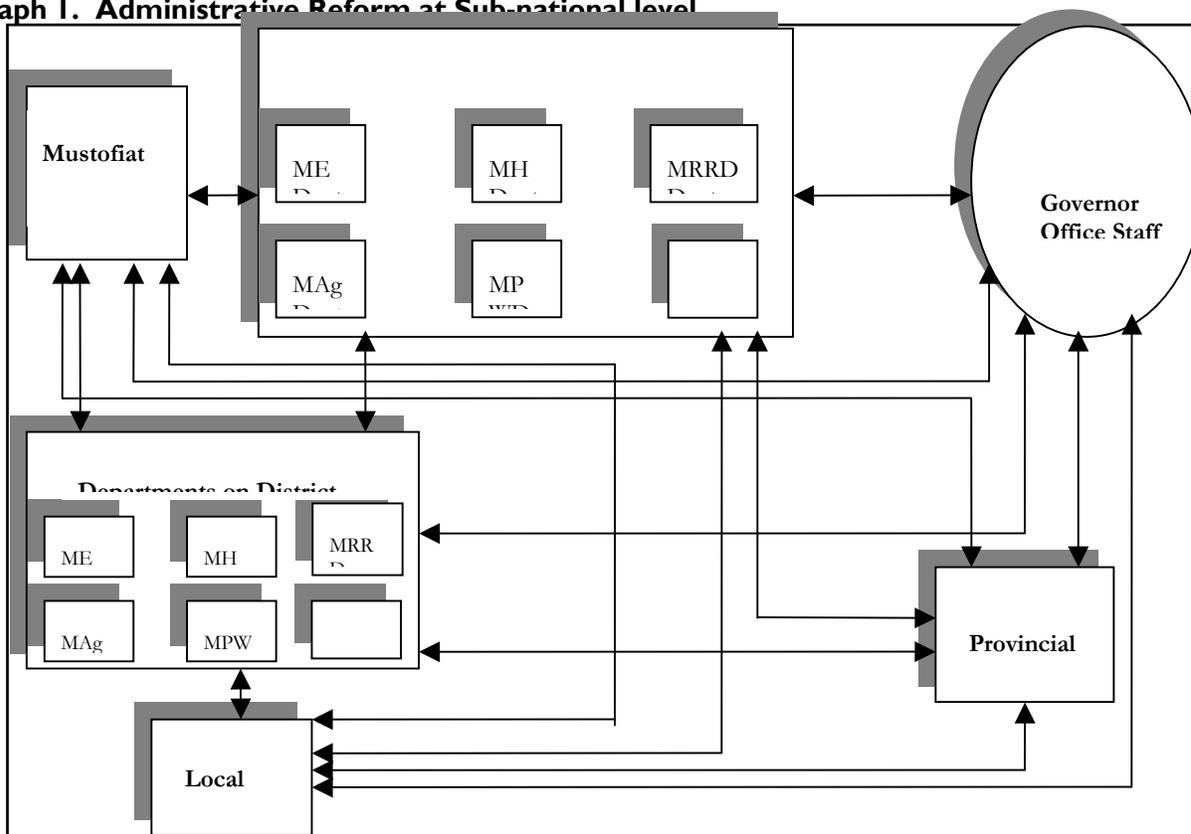
The main idea of the administrative reform is to separate political and directive functions (policy making) from day-to-day executive and operative tasks. According to this criteria, in each government agency there should be a Chief Civil Service (Secretary General) located outside of the political environment operating the system. On top of this, some new or even former staff carrying out strategic functions will be placed in higher salaries.

The whole reform will take time and resources as institutional and organizational changes must be understood within a long term perspective. Nonetheless, there is an ongoing quick start on a voluntary basis focusing on “core” units such as Da Afghanistan Bank, Customs, Treasury, Budget and the Office of Audit and Control. The PRR has been working within some critical ministries and agencies such as Health, Rural Reconstruction and Development and the Central Statistics Office. Advances and impact of the PRR is regularly monitored by a special unit that keeps the IARCSC and the MAC fully informed.

Now the PRR is moving toward working within provinces and districts. There is a logical sequence of reforms at the provincial level: from provincial departments to the Governor’s Office and then to cover the interactions between these two entities. Finally, there is the turn for Regional Councils, their structure and functions and the interactions with the previous two entities.

Work has been already completed in some provincial departments through their respective line-ministries. Now attention is given to provincial offices and functions. The main purpose is to review governors’ functions, eliminate duplications, establish work flows and change operational procedures, job descriptions and staff requirements. Appointments will be based upon merit and open competition. As reform makes progress in departments and governor office, there will be well- established procedures to interconnect these two. Governors will have a staff office to interact with District Offices and Councils. (See Graph 1).

Graph I. Administrative Reform at Sub-national level



Councils will be presented with some planning and budget authority, yet to be decided. Provinces and districts will have “autonomy” over a percentage of the budget which will be approved by Councils. Hopefully, these councils will exert fiscal and political control over the use of those resources.

The strategy contemplates five centers from where reform can be expanded. There is already a pilot program in effect in Balkh and four surrounding provinces and another one in Kabul. The next pilot program will be located in Herat.

The Balkh pilot program is underway (See Box 1). PRR has already covered the three main components of the process: an administrative structure that looks after development purposes, a new set of job positions (7) and the transformation of the old ones all of which are under the salary structure contemplated in the norm, and merit-based with open competition for the new positions which will be assigned by the CSC in Kabul.

All of these changes have certainly captured the attention of provinces. However concerns have been raised toward the political opportunity, the fiscal feasibility and the administrative effectiveness of the new administrative structure. Some see the risk of political capture of the PRR process by regional and local warlords, others worry over the lack of a reliable and sustainable source of resources and some others do not see any improvement in relation to the attention to those less able provinces and districts.

Certainly, the PRR initiative is a work in progress that leaves many unanswered questions and poses many challenges, especially for the ALGAP. The next sections consider diverse approaches to the problem and search for gradual and effective solutions.

3.0 PRESENT FINANCIAL MANAGEMENT FINANCIAL MANAGEMENT PROCEDURES AND PRACTICES: AN EVALUATION

3.1 EXISTING BUDGETING INSTITUTIONS: RESULTS AND INCONSISTENCIES.

3.1.1 Point of Departure: The AREU Report

Over the last years there have been great concerns about the capability of the government and particularly of the budget system to provide enough and timely resources to attend to payroll and non-salary expenses of provinces and district offices. This issue is not only about service delivery but also about endorsing loyalties to Kabul.

According to the WB (2004,c) operative organizations located outside Kabul and their staff have to cope with a budget system that:

- Delays payroll payments by weeks to a rather large number of organizations and by months to remote provinces and districts.
- Dispenses insufficient, almost nil, resources for non-salary expenditures to provincial departments and districts. This issue is increasingly resented as assignments disproportionately favor the ministries and agencies located in Kabul.
- Restricts cash flow thereby exacerbating execution problems, especially in those provinces which were used to retaining most of the national tax and customs revenues.
- Provides insufficient budget allotments for salary expenditures, particularly for the attention to workers in the social services.
- Assigns development resources through a distant, unclearly defined system that involuntarily promotes provincial inequalities.
- Presents very low salaries to civil servants, relatively quite below those earned under similar conditions by NGO's employees.

These issues are of great concern for the GoA which has been acting to solve them within its limited resources and strategies to reconstruct a unitary state. As it will be seen in next section, there are some remarkable achievements in improving the management and flow of public resources as well as some stubborn realities that are beyond the capabilities of a well working budget system.

Findings: advances in resource management and stubborn realities. Payroll delays have been appreciably reduced all over the country, though there remain some problems in remote districts. Actual payment delay is being reduced in all provinces to 10-15 days after the Treasury releases its payment authorization. For a country with as many communication problems as Afghanistan, this is a remarkable accomplishment. This was made possible thanks to a joint effort between the Treasury and the Afghani Central Bank. The Afghanistan Fund Transfer System (AFTS) transfers resources to Central Bank Branches located in twenty-nine (29) of the thirty-four (34) provinces of Afghanistan. The other five are attended to in nearby provinces or through telegraph services and physical cash delivery (See table 2).

Table 2. List of the Provinces/Cities where Afghanistan Funds Transfer System (AFTS) is functional

S/No	Province/City	S/No	Province/City	S/No	Province/City
1	Kabul	11	Kapisa	21	Samangan
2	Kandhar	12	Khost	22	Sheberghan
3	Jalalabad	13	Sharana	23	Nimrooz
4	Kunduz	14	Asad Abad	24	Baghlan
5	Mazar	15	Badakhshan	25	Logar
6	Herat	16	Taloqan	26	Zabul
7	Parwan	17	Maimana	27	Badghis
8	Gardez	18	Farah	28	Wardak
9	Laghman	19	Bagram	29	Ghor
10	Lashkargah	20	Ghazni	30	Panjsher

Note: AFTS is not operational in the following five provinces/cities but the resources are transferred there through the nearest AFTS point.

1. Uruzgan Province: The communication is taken place by telegram and they are using Kandahar AFTS
2. Bamyan Province: The communication is taken place by telegram and they are using Kabul AFTS
3. Nooristan Province: The mean of communication is available and they are using Kunar AFTS
4. Saripul Province: The communication is taken place by telegram and they are using Mazar AFTS
5. Diakundi Province: The mean of communication is available and they are using Kabul AFTS

As soon as the Treasury releases the payment authorization to provincial departments, on the 10th of each month, it also goes to the ADB which rapidly alerts the respective branch ensuring cash availability. Once the documents are reviewed by Mustofiat a check is issued to the respective departments which withdraws the money from the ADB provincial branch. The expenditure account is reconciled every month and the statement is returned to the Treasury for further review with the ADB.

Simultaneously, differences between the Tashkeel and the Takshis have been largely reduced as the first is being settled down by continuous examination and tight control by the MoF. Nonetheless there remain two types of unsolved difficulties. The first difficulty is related to the unexpected appointment of teachers to attend to the pressing needs for educational services primarily associated with incoming refugees. The second difficulty is the appointment of urgently needed bodies, usually related to security reasons, in the middle of the fiscal year without the respective funds.

Both cases show the weakness of budget institutions to control de-facto expenditures. As needed as these expenditures are, they show how to circumvent the system repeatedly and without consequences, until finally at the end of the fiscal year the MoF makes up for the excess of expenditures. It basically illustrates the need for better planning, more communication with departments but also shows an incapacity to enforce budget constraints.

One of the major accomplishments in the financial management area has been the successful efforts to centralize all tax and custom revenues in the Treasury. With the help of two independent accounts –revenues and expenditures- located at the DAB, the Treasury is running a centralized, unified budget. Tax and customs revenues are deposited in an account at the DAB which then regularly transfers those resources to the Treasury. Mustofies draw payments only on the expenditure account adequately replenished by the Treasury.

The new collection and payment system is a critical element in the process of building up overall central government authority and financial capability to attend - to greater equity thereby supports the demands of the population. The process naturally affected those provinces which were able in the past to dispose of those resources for the well being of their communities. This is an unsettled question so long as the budget allotments to those provinces do not match previous levels. An alternative introduced later on in this report

considers the possibility of allowing provinces to share in the marginal revenues coming from the establishment of a well working tax administration system throughout the country.

Many advances can also be registered in relation to the Development Budget though they are better understood against the broad review made by the World Bank (2004,b). Two mayor achievements can be cited in regard to the Development Budget. First, nowadays there are well established processes and instruments to prepare, evaluate and scrutinize technically sound projects which will then later be approved and funded by the Cabinet Committee. Budget execution of projects is organized and well kept through a Budget Contract Sheet that records contract characteristics, allotment requirements, advances and disbursements. Thanks to the involvement of the MoF (Budget Office) and the respective line ministry, the system is able to provide timely and reliable financial information.

The second achievement shows a relative reduction in the supply- driven expenditure pattern resulting from large participation of donors' funding in overall development expenditures through the MoF. With the new system, projects funded through the budget are structured around the development programs (National Development Framework and National Priority Programs). Still supervision by line ministries is quite weak and information provided for donors is rarely on time and seldom completed according to budget requirements making it almost impossible to analyze.

Though not an exclusive budget matter, low salary levels and what people see as an unfair treatment is becoming dramatic with everlasting consequences for the future. Provincial and district civil servants kept seeing salary increases for Kabul's staff while their claims and grievances were passed over. In this regard, recent administrative reforms introduced in Bakhl which carry a 400% percent increase to top officials' salaries, have developed a new wave of expectations which will be quite difficult to curb with more promises. Low public sector salaries carry with them unqualified recruitments with serious consequences for the quality of the service such as in the case of education in Bakhl. There most of the new teachers have not finished high school and they have reduced school time to go to the bazaar to earn a complementary salary.

3.1.2 Procedures inconsistencies and unsuitable practices

There is less bad news, but it is not less important for financial management outcomes. Operational and maintenance costs, those complementary expenditures required to keep organizations, people and machines performing at their best are insufficient. First, there is a lack of understanding about these expenditures in the whole productive process.. Recent research shows the effective participation of these expenses in all sorts of activities from social services to physical infrastructure. Second, governments and donors prefer investment projects that usually disregard the operation and maintenance costs associated with them. Finally, unfortunately, this type of expenditure permits easy transference to other purposes or easy cut off when fiscal conditions ask for budget sacrifices.

In spite of the achievements in the Development Budget, two weak links remain in the budget cycle that should be addressed before having a fully operational budget. The first of them is the so-called Policy – Budget link which arises in connection to the uneven technical capacity of line ministries to formulate and present projects to the Development Budget Office. This is aggravated by the lack of transparency existing in the selection and prioritization of those projects.

The second weak link relates to the lack of monitoring and evaluation of budget results. Individual projects in the development budget which are supposedly accessible for evaluation pass with little or no scrutiny. In addition there is an absence of any measure that relates current expenditures and accomplished tasks or goals previously established in the budget. The absence of an adequate system to examine budget results rapidly reduces it to purely an incremental exercise further severing the links between policy and resources and line ministries and their departments. Under these conditions there are few incentives to improve performance, much less to hold officials accountable for results.

On the revenue side the GoA presents two major success stories that deserve special attention for their impact over financial management and future sub-national activities. One of them is the reform of the custom collection process. There is nowadays a stable and comprehensive legal framework for customs; clearance times have improved; tariffs, exchange rates and valuation are closer to international practices and there is a growing enforcement capacity, especially at the borders. Simultaneously, there has been substantive effort to reorganize the central revenue administration. The creation of the Large Taxpayer Office in Kabul allows focusing on domestic revenue collection and compliance attention to the “top 100” entities in Kabul. Though previously mentioned, here it should be recalled the efforts to centralize revenues from taxes and customs by the Treasury. Certainly this productive effort can be corroborated by the performance of the revenue figures.

Though something of this sort is bound to happen at the provincial level according to the Five Year Plan³, present institutional and organizational conditions in Mustufiat have turned the tax collection in a purely voluntary transaction quite ineffective in revenue production terms. Legislative framework for tax administration is outdated and inadequate. Actual legal framework does not provide guidelines for self assessment; procedures for identifying, registering and keeping tax payers records do not exist. Nor are there provisions for accounting, review mechanisms or internal control. Mustofiat’s tax functions and authority over registration, licensing, control and collection is not well established, making the incorporation of new activities and tax payers within the administration control quite difficult. In many cases, a manual with tax procedures and processes was not even available. Existing old practices and on-the-job alternatives dominate tax collection procedures at the provincial level allowing for all sorts of inefficiencies and inequities as well as some corruption (Box).

3.2 CRITICAL ORGANIZATIONS AT THE SUB-NATIONAL LEVEL AND THEIR INTENDED AND UNINTENDED IMPACT ON FINANCIAL MANAGEMENT OUTCOMES

The starting point to evaluate the potential and effective contribution of sub-national administrations to the provision of social services is to locate them along the budget processes.

Table 3 shows the entities arranged according to the level of administration and their role in the financial management cycle. Basically sub-national administrations continuously manage well established and repetitive tasks that do not demand new knowledge or extraordinary effort. For the budget they prepare the payroll and once it is cleared by the Mustafiat they proceed to pay the staff. When resources are available, and according to the amount to be expended, they prepare a joint bidding process with the Mustofiat and the Governor’s Office to acquire the needed goods and services. Basically they are merely operators in a highly centralized administrative structure.

Table 3. Budget Procedures and Government Organizations			
F.M. Procedures	National	Provincial	Districts
Planning	MoF DB, OB		
Assigning	Cabinet, MoF, Mol, LM.		
Approval	Cabinet – Parliament		

³ The Way Forward. A five Year Plan (2004-2005). Ministry of Finance GPR. Kabul, December 2003.

Execution	Order	Treasury		
	E C		Mustofiat	
	P		Departments	Districts
Acc & Reporting		MoF, Treasury		
Evaluation & onitoring			MoF, LM, Departments	
Control (Audit)		MoF		
Note: cabinet approves nowadays but in the future the parliament will approve it EC=Expenditure Control P =Payment				

Table 4 presents a primary valuation of the functional and managerial capabilities of the aforementioned entities. A scale of 1 to 10 was employed to qualify all organizations. The exercise established the following four factors characterizing the organizations' capabilities:

- General capabilities and operative conditions deteriorate top-down, from the MoF to districts, especially in relation to operative conditions.
- Operative working conditions deteriorate more rapidly than technical knowledge and required skills.
- Knowledge and technical capabilities to carry on new tasks are nonexistent.
- Differences in knowledge and capabilities and even in operative conditions between provinces grade 1 and provinces grade 2 and 3 are abysmal. The same is true for districts.

Under these conditions public resource effectiveness, depends mainly on the decision making institutions and the high ranking directives. Sub-national entities' contribution depends basically on the amount of resources assigned for operation and maintenance costs and on the accountability exerted by the provincial government and by line ministries which is nil in both cases. Efficiency in terms of low production costs is out of the picture given the lack of autonomy over resources and the lack of interest in accountability on the local level.

	ORGANIZATION	OC	K	S	A	IT	T	WC
	Central G							
	Treasury ¹	9-5	9-4	8-4	7	6	6	7
	DB	9	8	8	9	9	9	7
	OB	8	8	8	8	5	6	6
	Mol	6	5	5	4	4	4	5
	MDH	5	4	4	4	3	4	5
	MG	8	8	8	7	6	6	8
	Provincial Ad.							
I.	Mustofiat	7	4-9	4-8	7	4	3	3

	AG	7	7	6	7	3	3	3
	IRR	8	8	7	7	3	3	3
	EDUC	9	9	8	8	4	4	4
	G.O	7	6	6	7			
3.	Mustofiat ²	6	4-6	1-6	5	2	2	2
	AG	7	6	6	6	3	3	2
	G.O	6	5	5	4	4	4	5
1.	District		6	6	7			4
3.	District		5	4	5			3
Note: Directive and Operative personnel Qualifies technical abilities to handle tax and budget expenditures OC: Organizational Culture, K: Knowledge, S: Skills, A: Attitude, IT: Info Tech, T: Tech, WC: Working Condition								

A search for greater effectiveness and efficiency must take into account the above mentioned institutional deficiencies in planning and prioritizing investments and operational and maintenance costs, the functional capability of entities and the need to create some intergovernmental accountability mechanisms. For greater delegation of functions, this report emphasizes the need for some local fiscal effort that must be combined with greater community participation and accountability for pre-established results.

4.0 RECOMMENDATIONS FOR INSTITUTIONAL ADJUSTMENTS AND GUIDELINES FOR TA&T

4.1 GENERAL STRATEGY TO IMPROVE FISCAL AND FINANCIAL MANAGEMENT WITHIN A SUB-NATIONAL PERSPECTIVE

In the last three years of state-building in Afghanistan, the Budget has been a critical instrument for policy making as well as for coordinating funding activities with donors. Nowadays there is a budget system that centralizes all tax revenues in the Treasury, programs and assigns annual and quarterly allotments with fairly good accuracy, releases funds and attends to timely salary payments to public officials all over the country. A Financial Management Information System is being put in place making available accurate information on financial budget expenditures and accounting reports which is a remarkable achievement in such a short period of time for a country at the verge of collapse.

Nowadays, the GoA is moving its attention towards the effective provision of public goods and services through an enhanced role in the process for sub-national administration. The ongoing administrative, fiscal and financial management reforms and even the political reform all coincide with the need for a gradually more tough delegation of competencies and resources to those regional and local entities. This should be followed by further concentration of central government functions, on policy making, coordination, and evaluating results, slowly delegating operational matters to sub-national administrations.

It could be said that budgeting in Afghanistan is entering a stage of what constitutes an effective system of public financial management which simultaneously searches for fiscal discipline, strategic prioritization of resources and effective service delivery. From now on budget procedures and practices should look after the delivery of more and better social services (outputs and results) rather than merely on fiscal and financial macro stability.

This is a pretty ambitious undertaking for a country that simultaneously faces organizational and institutional obstacles and growing political pressures amid a very tight fiscal situation.

Conditions call for a comprehensive though gradual strategy driven through a three pronged approach that includes:

- A bottom up component design for enhancing managerial capability of provincial and district officials with the help of Technical Assistance and Training provided in close coordination with the ongoing PRR reforms advanced by the IARCSC and the DID program.
- A top-down component in charge of formulating adjustments and promoting options for those financial management procedures and practices that limit a more effective participation of sub-national administration in the provision of social needs.
- Continuous and unstoppable efforts to enhance (create) accountability relationships between the actors related to the provision of public services. It has been repeatedly proven that improving the delivery of basic needs requires more than human and financial resources; the key actors –political bodies, government and public- need to be accountable to each other. Initially this component focuses on intergovernmental accountability while building up instruments for political and public accountability of governments.

4.2 FINANCIAL MANAGEMENT INSTITUTIONAL ADJUSTMENT.

To consolidate observed progress in effective budgeting complementary efforts have to be done in three fronts:

4.2.1 Public Finance and Expenditure Management Law.

The GoA is proposing a law which draws together all the innovative budgeting institutions that help explain its success. At the core of the budget law, there is a cash management system that regulates allotments and expenditure authorizations throughout the government preserving tight fiscal discipline.

The proposed law certainly covers most of the multiple “dimensions” for a public expenditure management assessment under the Public Expenditure and Financial Accountability Program (PEFA) (for a detailed analysis see appendix A1). However, there are some elements of the proposed law that deserve further discussion, especially in relation to the following eight areas: first, to the unbalanced role assigned to the Treasury in detriment of the budget function and the follow up of budget outputs and outcomes; second, to the unfinished mechanism for programming and assigning resources to programs and projects within the development budget; third, to the second class treatment to operational and maintenance cost and the unpredictability in the allotment and execution of those resources; fourth, to the differences between the role assigned to the Mustofiat in this project and the ongoing reform being done by the Revenue Office of the MoF; fifth, to the inadequate treatment granted to intergovernmental fiscal relations and the inappropriateness of the Mustofiat to manage them; sixth, to the excessively soft approach towards donors’ aid which leaves reporting almost on a voluntary basis and makes any possibility of monitoring and evaluation of those resources disappear; seventh, to the lack of technical instruments to establish outputs and to hold officials accountable for results; and finally, to the confusion of the role assigned to the Secretary General of the Ministry which should be clarified.

4.2.2 The weaknesses of some of the links of the budgeting cycle and their impact upon an effective budgeting system.

In the budgeting cycle initially community needs press for policy answers that later become budget assignments. These assignments once executed must produce outputs that should match the initial needs that triggered the government action. Despite the completed efforts made by the GoA two difficulties remain in the budget system that should be addressed before having a fully operational budget.

The first relates to the uneven technical capacity of line ministries to formulate and present projects to the MoF (Development Budget Office) and the lack of transparency in the prioritization and selection of those projects. In this context it is necessary to improve the technical capacity of line ministries and of their provincial departments enabling them to prepare sound projects. It is also necessary to clarify the criteria and processes employed to select projects as well as to make the results public by sector and province.

The second associates with the lack of monitoring and evaluation on the expected and observed budget results. The Financial Management and Public Expenditure Law bring in the responsibility for Ministries and government institutions to reach the objectives and outputs approved for each program (article 14). The law also establishes the instruments for following up and auditing the process. Not much has been done to develop this mandate; responsible officials do not have clear directions on how and when these dispositions will start working. Here, there is a big challenge to transform an input oriented budget into one that searches for outputs and results. Technical assistance and personnel upgrading is required to carry out the mandate of the law.

4.2.3 Pressing realities and needs for a fully operational financial management system.

Unfortunately budget systems cannot be purchased in a store. They are “works in progress” that continuously develop according to changing political, economic and social circumstances. Reforms do not implement themselves, in most cases a group of experts lead and coordinate the effort. In the case of Afghanistan, there is a pressing need to ensure the active presence of well trained local experts to gradually take over the macro reforming process occurring in the Budget Office and in the Treasury.

This need for reinforcing local expertise becomes more acute once attention is directed towards the state of basic supporting subsystems. Without these subsystems such as forecasting, program and project selection, budget examination, accounting, monitoring and evaluation and information and aid management, the budget system is unlikely to perform well much less be sustainable in the long run. This report found most of these basic subsystems in embryonic stages quite far from full service. The demand for well trained officials becomes more critical when considering the splitting reforms to the Mustofiat introduced recently by the revenue office and the treasury.

4.2.4 Parliament and Regional Councils and the Budget.

Parliament’s concerns are about taxes and expenditure decision-making. Altogether the limited role in budget preparation assigned in the Constitution and the prevailing fiscal conditions in Afghanistan will disconcert most of elected MP in next September. There is the risk as acknowledged by the WB (2004,b) that disenchantment with budget figures and issues result in its disengagement from fiscal and financial management issues or in an endlessly political feud too costly for the country.

Building on the WB recommendations and on findings in this report the ALGAP could contribute to lessen this risk by:

- Building up MP’s capacity to deal with fiscal and financial affairs and exposing them to similar experiences in other countries.
- Providing the Parliament with accurate, appropriate and timely information as well as with documentary explanation of tax and spending proposals.
- Defining expected outputs and results for programs and projects in the budget and, in this way, facilitating the understanding of government policies and their adequate control.
- Establishing a small technical unit able to monitor and evaluate strategic programs during their execution.

Provincial Councils presents a similar problem though of greater proportions. The disenchantment of provincial councilors could be worse since there is not a provincial budget neither there are own resources to dispose off. Initially, councilors could help in controlling the flow of resources to departments and districts established in the national budget and evaluating the results obtained with their employment. Later, as the process advances, they could play a more relevant role in evaluating and controlling provincial government investments and projects as well as developments at the district level. It will be quite interested to acquaint them with the role of state councils in neighbor countries and on intergovernmental fiscal relations.

4.3 OPTIONS TO ACCESS THE DEVELOPMENT BUDGET AND TO INCREASE “OWN” RESOURCES FOR SUB-NATIONAL GOVERNMENTS.

Despite all previous considerations on institutional reform and the incomings on organizational strengthening the plain truth is that without fresh resources there is little to be done to improve the provision of public services nowadays in Afghanistan. This is an unavoidable truth well known and overly present in central government decisions and results. The following considerations, with the exemption of the one related to

operational costs and maintenance, begin with the principle that all suggestions to improve the delivery of social services must be kept within the limits imposed by the fiscal limits or to propose a mechanism to raise a significant portion of the resources needed.

4.3.1 Operational cost and maintenance.

Much can be done to improve the coverage and quality of the State services by providing adequate resources to operate and update the relatively large and still standing provincial and district state apparatus. Sectoral departments and sub-national administrations still provide valuable economic, social and political services well below present market prices or at least NGO's prices.

In this regard, it will be quite useful to closely evaluate the process followed by line ministries to assign those resources and to improve the capacity of the MoF to review their demands. The annual allotment to provincial departments established this fiscal year 1384 contributes to this goal and gives the opportunity to introduce some accountability for outputs.

More has to be done in this front. It will also be useful to find out the amount of resources needed to operate some of the most critical services and assign them or part of them against explicit results. The respective Ministry should lead a "joint" governmental effort that includes sub-national administrations which will be then accountable for achieving the pre-established results. It will not only allow government to reap the benefits of fully using idle capacity but also enforce accountability throughout the government bureaucracy. Similar projects were explored in the Ministries of Education and Agriculture with great perceptibility and willingness to join efforts with the ALGAP.

4.3.2 Direct access to the development budget or to Donor's resources.

Some projects presently being carried on by NGOs at the provincial level are within the technological reach of provincial departments but managerially beyond their capabilities or those of the provincial administration. There is the possibility for provinces, mostly grade 1, to enhance their technical and managerial capabilities, enabling them to direct and manage mid-size and low complex projects. Ongoing PRR reforms of provincial governments (see Bakhl above) and departments led by the IARCSC seem to be pointing towards this type of outcome. In that situation there is a pressing need for technical assistance and training, especially in project financial management which could help to ensure the success of this type of endeavor.

Dealing with provinces grade 2 and 3 require a different approach. Paradoxically, size, complexity and costs of attending pressing basic needs overwhelm the scarce technical, human and financial availability of resources in those provinces. The same elements conspire to put them away from the traditional paths traversed by donors and even by the same national development budget. Technical requirements for project consideration overkill any chance for those provinces to be heard in those spaces.

Replicating PRR's reform in Bakhl will serve other purposes but certainly it will not give voice to those provinces in the political, technical and financial arena where decisions about the development budget are taken. In this regard it will be quite useful to recall a proposal made in the World Bank-AREU joint report (2004,c) where a cross cutting consultative group will be in charge of elaborating and presenting technically and financially sound projects to improve social service provision in second and third grade provinces. This and some variations of this type of intervention will help to eliminate provincial isolation from the budget and will certainly help to reduce regional inequities.

4.3.3 Conditional grants from central government.

In the Public Finance and Expenditure Management Law the GoA explicitly introduces the possibility to transfer budget resources to municipalities (articles 64-65). It recognizes the importance of these entities in the provision of public services as well as their operative and management capabilities. It may take some time for provinces to access a similar type of treatment. Meanwhile there is the need to build up their managerial capabilities and to promote joint efforts initially around specific projects with the provincial departments.

4.3.4 Increasing collection of taxes at provincial and local level and a sharing proposal.

All tax revenues, with the exception of municipal taxes, belong to the central government of Afghanistan. Tough districts collect some tax revenues –land and small business taxes-, provincial governments are purely secondary budget units without any tax or expenditure authority beyond their allotments assigned by the MoF. Nonetheless, any further delegation of functions and transfer of resources to do so, should not go unaccompanied by some self effort to participate in the search for greater revenues.

This is advisable under several grounds: first, there is the stringent fiscal limit already mentioned; second, costs of local goods are easily related through benefit considerations to fees and user charges or even to specific taxes such as the gasoline tax and road maintenance and construction and third, larger local contributions incentive accountability and search for efficiency in public agencies. Moreover, taxes do not have to be owned or collected by provincial authorities; in cases like this it is used to establish a share over marginal revenues.

Ongoing reforms of the Mustafiat, promoted by the revenue and the Budget offices of the MoF present the government with the opportunity to build up revenue consciousness with greater delegation of functions and budget transfers to sub-national administration. Among the many objectives proposed in the Five year plan of the MoF 2004-2008, General Presidency of Revenue (GPR)⁴, is a set of fully functioning provincial administration offices that are separated from the budget execution agencies in the Mustofiat. These offices will manage all taxes and taxpayers of the province connected to few (5-7) large size regional offices. Bluntly it means greater tax pressure which could be better accepted if connected with the funding of some specific activities.

This is a long term project with decisive impact over the viability and sustainability of the fiscal and economic strategies of the GoA. Besides this critical point, this reform will dramatically affect the possibilities to increase the funding and thereby the provision of public goods and services and the effective participation of sub-national administration in the process. Considerable part of its success depends on the availability of experts and well trained officials able to administer a modern revenue administration. Technical Assistance and Training requirements are over us \$ 12 million covering subjects such as organizational change, law reform, human resources management, ethics, accountability and internal assurance, work practices and technologies, accounting, auditing and many other technical and managerial subjects. A related sub-product arises with the possibility of rapidly transferring expertise and skills to districts and municipalities. Initial conversations held with the Customs and Revenues Deputy Ministry allows a vision of a large role for LGAP in the proposed reform if desired.

The above is a complex project programmed to take place in five years, but is still subject to some critical decisions that may deter its implementation. Districts present an expedient opportunity to develop a tax management reform that will be easier to implement as long as the increase in revenue collected remains in the district.

⁴ The Way Forward. A five Year Plan (2004-2005). Ministry of Finance. GPR. Transition Islamic State of Afghanistan. Kabul, Afghanistan.

Districts collect taxes on land property (suspended a few years ago by the MoF to ameliorate the drought impact), land transactions and on small shops and businesses. Districts also receive yearly fees for leasing the district's lands. These resources are duly deposited in the corresponding Mustofiat's account.

The Districts' taxes barely represent over ...%, of total national revenues. These taxes are collected purely on a voluntary basis. Tax payers have no incentive to pay them nor the district officials to collect them. Lack of accountability further holds back efforts by both sides to fulfill their respective duties.

Within the context of financial management reform it will be very useful to prepare a project that includes the procedures and complementary elements to improve tax collection and local budgeting at the district level as well as the training needs to carry them out effectively. However, the reform should include the opportunity for the districts to assign those resources to attend to basic needs being overseen by community organizations.

This institutional arrangement allows for the benefit incentive to fully take place while local overseeing and accountability change it to a self-contained tax-expenditure arrangement.

4.4 STRATEGY, TIME AND SEQUENCING FOR FINANCIAL MANAGEMENT REFORM

The main purpose of this assessment is to review and establish procedural strengths and weakness in public expenditure management from a sub-national perspective. This analysis provides the basic elements on which to develop and implement action plans for adjusting or reforming legal and institutional budget structures as well as for building human and organizational capacity in those entities involved in the budget process. This report adheres to the three basic principles for viable reforms: i) it is country specific and its feasibility is inherent in government priority and overall strategic setting, ii) it will be enacted upon final government choice and formulation, and iii) it will attend capacity building through processes, on- the- job training and with coordination and participation of responsible entities.

As for the sequencing and timing of the reforms, the bottom line for improving the provision of public services is to be found in the availability of resources, and the institutional and organizational arrangement and time frame to apply them as chosen by the GoA. The choice will define the main actors of the process, their roles and the need to adjust or reform financial management institutions. It will also define what, when and how competencies and resources are to be transferred and thereby the type of administrative structure and capabilities required by sub-national administrations to fulfill their new roles.

Until this time and mostly based on scattered facts and evidence, this report perceives the intent for a gradual, long term shift from a highly centralized government directly involved in the production of those goods and services toward a de-concentrated political and administrative structure. According to this scheme ministries will gradually and selectively, by province and sector, give up most of their operative functions to provincial governments, districts and municipalities. Under this arrangement, there should be an initial period of central government strengthening focused on procedures for planning, tax collection, and monitoring and evaluation of results. It is expected that once they are in place, then there will be a decisive move toward transferring resources and competencies.

Until new evidence on the government's purposes is put forward, this report holds to a sequence for ALGAP's intervention that focuses initially in removing the institutional obstacles that impede present arrangement for resource mobilization and their allocation to strategic priorities as well as their follow up and evaluation of results in the central government. Then, attention is provided to financial management in provincial municipalities and accordingly their options to improve it. This goes along with some efforts to improve tax collection and reporting at the district level. Finally, there are some efforts to build up provincial government capacity to develop, implement, monitor and evaluate projects. The latter effort will completely change if there is some signal from the government to press on the tax collection at the provincial level.

The reform process begins with the identification of processes and practices that disturb financial management outcomes, particularly those related to effective prioritization and allocation of resources and efficient delivery of social services. After establishing the causes of the difficulties: a lack of or insufficient legal framework, procedural inconsistencies, misplaced or inadequate incentives, outdated administrative structure, the strategy considers the presentation of several alternatives to remove the institutional and organizational obstacles. Then, follows a period of discussion and consensus building where stakeholders are brought together in order to participate in the solution. Once a decision is made by the government, there comes a period of implementation designed according to the particular reform.

The following Action Plan covers all the different elements and stages contemplated in the strategy for institutional reform:

- Stage 1. The main purpose here is to identify the institutional weakness and obstacles that impede effective financial management within the central government and the sub-national administrations. Budget procedures for programming, approval, execution, accounting, reporting, monitoring and evaluating and control are evaluated in terms of fiscal discipline, allocation of resources to strategic priorities and managerial efficiency in delivering social goods (see questionnaires Q1). Table 5 shows the budget institutions arranged by administrative level that should be addressed to improve public financial management.
- Stage 2. This stage is about elaborating remedial actions and proposing them for discussion with government officials. An initial set of interviews, exercises and field reviews conducted under this assignment allowed for identification of some causes and disincentives for critical failures in budgeting procedures and practices. Though further research is needed to confirm these findings, table A advances some remedies as well as actions proposed to remove the failing procedures.
- Stage 3. This stage provides the scenario for discussing alternatives with stakeholders and for building a consensus around specific solutions before submitting them for government approval. In order for reforms to work, they ought to be appropriated by responsible officials, operators and by beneficiaries. Otherwise proposed changes do not go beyond being a purely conceptual exercise. Initially the strategy considers a set of arm's length discussions with relevant policy makers to test the effectiveness of the alternatives proposed. There will be some seminars and workshops to examine the proposals and to gain stakeholders' advocacy and government approval.
- Stage 4. Once reform is approved, this stage provides the resources for the diffusion of the new norms and procedures as well as the TA&T required for implementing them. Chart OPA shows specific tasks, operative details and a tentative timeframe in which to carry out the institutional reform.

Table 5 Financial Management Procedures to be addressed by ALGAP		
NATIONAL	PROVINCIAL	DISTRICT
MoF FMPE Law Criteria for Approval Projects Procedures for Screening Projects Elements to Assign OC&M Procedures for Tax Administration Procedures and Instruments for M&E Basic subsystems: Accounting, Auditing, Reporting L.M Project Design & Formulation And M&E Parliament FMPE FI (Literacy) Decentralization (RD) Audit – Accountability Policies	Mustofiat Expenditure Control (Tashkeel Payments) Tax Administration (P- D) G.O Project Design & Formulation and M&E (Audit) Project Implementation Provincial and regional planning Departments Project M&E Implementation R. Councils * Joint Activity/Requires Reforms	Districtics Tax Administration Accounting & Reporting P. Planning & Community Project Management Municipalities Strategic Planning Tax Administration Budget Management Public Service Mngmt.

4.5 GUIDELINES FOR TA&T TO IMPROVE STAFF AND ORGANIZATIONAL EFFECTIVENESS IN MANAGING PUBLIC RESOURCES (SEE PROJECT MANAGER CHART I).

Performance depends on several grounds going from adequate macroeconomic conditions, through stimulating institutions, adequate governance structure all the way to individual's knowledge, skills, attitude and incentives as well as on technical support and working conditions. The report has already been able to deal with some of the macro and institutional and organizational variables that affect performance. Now it turns to on the job qualities and surrounding environment that make civil servants more or less productive within a specific organization. Once these elements are fully identified, the purpose is to design and provide the TA&T required improving staff and organization effectiveness in managing public resources.

Table 6. Organizations and TA&T Assistance by ALGAP		
NATIONAL	PROVINCIAL	DISTRICT
MoF FMPE Law: IR DB – OB: IR T: TA & T General Basics:TA & T TM: TA & T L.M B & PI Off : TA & T Parliament	Mustofiat EC: TA & T TM: TA & T G.O Project Design & Formulation and M & E: TA & T Departments Project Design & Formulation and M & E: TA & T R. Councils	District Tax Management: IR & TA & T Acc. And Rep: TA & T P Management: TA & T Municipalities Strategic Planning Tax Administration Budget Management Public Services Mgmt.

FI: TA & T	TA & T	
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- Stage 1. In this first stage the main activity consists in identifying agencies and their real capability to carry on with financial management procedures and practices. This set of entities does not necessarily coincide with those listed for institutional reform. Here, the agents refer to those entities and the specific offices where clear deficiencies or vacuums in financial management have been detected e.g. District Financial Office, Provincial Government, Mustofiat, Provincial Municipality Financial Office (Treasury), Budget and Planning Office in Line Ministries, MoF, etc . These entities are divided into three categories according to the established priority to receive TA&T.
- Stage 2. The second stage is about singling out staff's qualities and capabilities and the working place's technical and physical conditions that help to explain an organization's performance deficiencies and unintended results. A questionnaire is being designed though not yet proven, to establish the following: knowledge of norms, functions, procedures and practices, job's required skills, officials' attitudes and perceptions of incentives, technical and technological support, working conditions and organizational culture. An initial exercise permitted to establish a tentative set of organizations where TA&T would be provided by ALGAP (Table 6).
- Stage 3. In this stage the program will provide specific remedial technical material such as new and more effective procedures to carry out functions, needed skills and complementary capabilities for on-the-job performance; the program will also provide recommendations for more effective IT as well as on technical equipment and physical working conditions. These activities will be coordinated by and consulted with the responsible authorities and conducted as much as possible under the direction and auspices of the IARCSC.
- Stage 4. In stage four there will be a joint effort by ALGAP and well known experts to design the training strategy, elements and logistics for each of these organizations. The strategy will provide a national coverage within a regional or provincial context. Here it is expected to establish relevant training methods according to content areas, prepare training material with clear objectives and expected results and relevant indicators to evaluate them. All of these elements should be part of a detailed training plan which should also include participants, norms of behavior, time schedules and so on.
- Stage 5. In the last stage training will take place according to a general plan which should follow strategic needs and organizations. Implementation will be carried out by TA&T experts under the coordination and supervision of ALGAP. TA&T will gradually cover all regions and chosen entities and officials. Observed results and continuous evaluation will help to rapidly incorporate corrections and changes in the program.

5.0 PUBLIC FINANCIAL MANAGEMENT IN PROVINCIAL MUNICIPALITIES: A GUESSTIMATE

Finally, financial management is about planning, executing and controlling public revenues and expenditures. The central government is one of the two governments in Afghanistan that have the authority to collect and spend public resources, the other one is the municipality government, particularly provincial municipalities. Though not contemplated in the TOR for this assignment, any further consideration about local participation in the delivery of public goods and services should include municipalities. This is not a comprehensive analysis of municipal financial management. It is just an initial guesstimate of institutional strengths and weakness of three main provincial municipalities and which also explores some institutional and organizational elements that could improve the coverage and quality of local public goods and services at the municipal level⁵.

5.1 ELEMENTS FOR FINANCIAL MANAGEMENT IN PROVINCIAL MUNICIPALITIES:

5.1.1 Existing legal and institutional framework for municipalities, responsibilities and organizational structure.

Municipalities, according to the Law () are independent institutions required to provide for the needs of its local population. Authority resides in the Municipal Assembly which is an elected body of no less than five persons but no more than 20 according to municipality size. The Assembly elects the mayor and other high ranking officials and may form a council with the participation of some of its members. This council has some administrative and control functions.

Municipal responsibilities cover all sorts of community assistance, attention to social needs, and provision of urban infrastructure and development of productive activities. Municipal duties stated in the law range from the attention to health conditions, to the construction and management of water, sewage and garbage disposal systems, to building permits and housing provision. The law also considers the construction of horse racing fields and stadiums, price controls, ice-making factories all the way to the preservation of environment conditions and cultural and social amenities.

Though some of the existing infrastructure was built by the central government under the scheme of the Master Plan's development, municipalities have made a great effort to improve coverage and quality of services. Water supply and sanitation is a good example of this type of intervention and its enduring results. The Central Authority for Water Supply and Sewage (CAWSS) is responsible for urban water supply and sewage, with the exemption of Kabul. The other two main cities, Mazar and Herat, are responsible for their own water supply.

Despite central government intervention, coverage and quality of water supply in Afghanistan is quite low and differs widely among the provinces. Compared to its surrounding countries, Afghanistan shows the lower access to improved water sources (40%); in this group Turkmenistan shows the highest coverage (92%). Coverage and quality vary widely among provinces and cities. Piped water barely represents 7.7% of drinking water sources; over 20 provinces do not have this service showing enormous water safety and correlated

⁵ This section is based upon the stories of three cities: Kabul, Mazar I Shariff and Herat, their institutional framework for financial management and their experiences and outcomes providing public services.⁵

health problems. Municipal coverage of piped water is quite a bit higher than the national average; Mazar's piped water coverage is 46.8%, Herat's and Kabul's are 39.4% and 36.2% respectively⁶.

5.1.2 Budgeting institutions and management.

Municipal Law includes a very well developed set of institutions –norms and procedures- that cover practically all stages of the budgeting process. In chapter eleven the law establishes the requirements and processes for tax assessment, allowed expenditures, current budget constraints (less than 40% of FY's income), budget presentation, approval and execution. It also specifies accounting procedures and responsibilities and final reporting and auditing. Once the budget is approved by the Assembly, it is sent to the MoF for confirmation. If the current expenditure budget exceeds the 40% limit, it requires MoI approval.

With some small differences budget procedures in Mazar and Herat are quite similar. In both cases they basically follow up on established procedures. As it will be seen in next section, Herat keeps its focus on a small number of strategic objectives while Mazar presents a wide choice of expenditure commitments. The latter presents great reliance on incoming central government funds. The striking factor is the presence of a continuous fiscal surplus in both cities. While Mazar closed 1383 FY with a surplus \$ 58 million afghanis in the ADB, Herat shows a \$ 30 million surplus. A similar result is observed in the World Bank study (blue AREU) for all six cities in the sample.

Stringent budget controls for current expenditures and reluctance of MoI to approve any salary increase and Tashkeel expansion helps to explain this recurrent but not obvious result. To explain the fiscal surplus, there should be also considered the weakness of the municipalities to establish sound tax assessments and their lack of capable planning office. Municipalities should not be producing surplus under present levels of coverage and quality of local public services, but it would be quite acceptable for them to remain fiscally neutral, as recognized by the PFEM law. This is an important issue that it is addressed in next sections.

5.1.3 Tax and revenue collection

Municipalities (Herat and Mazar) collect a fair amount of resources that are enough to attend to staffs' salaries, operate and maintain some basic services and build critical urban infrastructure. In regard to tax structure and tax collection, municipalities are not as independent or autonomous as the law may want them to be. Authority over taxes finally resides in the MoF which may eliminate, suspend or modify taxes according to the national interests without consulting or providing income alternatives for the affected entities. Herat finances were largely affected by the suspension of the tax on vehicles; Mazar could not obtain MoF's permission to update cadastre values and both of them suffered a great setback in their finances with the centralization of custom's revenues.

Tax structures are similar in both cities. Their incomes basically depend upon user charges and fees for commercial activities and services, rental of shops and other municipal properties and a tax on private house leasing equivalent to one month's rent. However, each city has followed a different path to buttress their revenues against changing rules and according to their specific circumstances. Over time, the city of Herat has become a room and board and wedding facility entrepreneur as well as the owner of many commercial rental properties. Both activities produce a yearly income of \$ 59 million afghanies, equivalent to 58%% of the 1383 FY budget. Masssar has followed a more conservative path although business rentals represent over 30% of its income. Nowadays, this city is trying to put up a land development project which may bring substantive income gains.

⁶ Afghanistan Statistical Yearbook 2204, pages 79 and 97.

Despite their differences the representatives of both cities recognized the need to increase local revenues as well as the technical and administrative weaknesses of their tax collection systems and the need to improve them. Procedures to identify tax payers (census) and tax base and obligations, principles for tax assessment and ruling and mechanisms for review and dispute resolution and internal controls are either outmoded or do not exist. Enforcement power and instruments for tax collection are held by the MoI. Accounting is done manually and even though it follows procedures it is not written, leaving bookkeeping and reporting dependent upon personal recalls. In any case one year old records are beyond scrutiny. In both cities there is an urgent need for technical assistance and training of officials to revamp tax administration and revenue collection.

5.1.4 Planning and Master Plans.

According to the law, municipalities are responsible for planning. Though the Master Plan concept stills dominate the scenario, planning is rapidly moving towards a more strategic concept. Three years ago the newly elected mayor of Herat decided to modify the old Master Plan and focus on the solution of two strategic needs: the expansion and maintenance of the water supply and drainage system and the paving of streets and construction of parks and recreational areas. He rapidly gained the community's support which was later solidified through a compensation scheme that reimbursed the community for 60% of the properties affected by road construction. Resources came from charging and collecting rents for the municipality's properties and from revamping the entertainment and boarding businesses.

Mazar is working with the Ministry of Urban Development and Housing in a Master Plan that contemplates land zoning, water supply and sewerage systems, planning of new streets and avenues, and the construction of schools, public buildings and recreational areas. The Plan also includes administrative reform and staff upgrading. Once it is completed, it will be taken to the Council of Ministries to be approved; then it will become the City Plan.

The PRR under the IARCSC is developing an administrative reform model in Kabul that would be replicated in other cities. The purpose is to "reform" the municipality and focus it on improving service delivery. The reform promoted by the PRR –SERAP considers three stages:

- Stage 1. It engages high top officials (mayor and deputy mayor) in the Administrative reform process.
- Stage 2. It designs and introduces a set of measures fully aligned with the NDP plan: i). Strategic Plan, ii) New Organization Structure, and ii) Meritocracy as base of recruitment of high ranking officials.
- Stage 3. It triggers municipality into solving own problems starting with a mayor project.

Fiscal and Financial management is a critical component to be considered in stage 2. This is a holistic approach where the generation of own resources are fully integrated into the Strategic Planning. Increasing revenues will enhance governance through greater expenditures and accountability of local authorities.

Besides the administrative reform, the CSC is also considering to transfer to municipalities the responsibility over local police and traffic. CSC wants also to divide responsibilities toward "housing" with the Ministry of Urban Development and Housing. The Ministry will keep policy making and direction functions while municipalities will be fully in charge of housing.

An interview the Minister of Urban Development and Housing recognized that planning methods are rapidly changing in Afghanistan. The new methodology includes a vision of the municipality in the near future, a mission to be carried on in the context of pressing needs and possibilities and within a regional and environmental perspective. A strategic plan identifies and plans for the provision of few critical factors –water systems, transportation needs and services- that will allow for a business and social enabling environment. This means devolving to the municipality some of the functions which were assumed by the central

government in the past as well as strengthening their financial and administrative capability. Strategic planning demands an active role from community within a good governance scheme.

This vision contrasts with the top-down, comprehensive planning of the Master Plan quite improbable to be implemented. The Minister also acknowledged the lack of technical capacity to elaborate the MP even for a few large cities. Under present conditions, the Minister considers it more useful to strive for short term zoning plans with a strategic element and definitely with community participation. There remains of course the political and economic interest to keep tight control over municipalities traditionally protected by the Master Plan concept.

5.2 GUESSTIMATE ELEMENTS FOR FURTHER INTERVENTION AND DESIGN OF A PLAN FOR TECHNICAL ASSISTANCE AND TRAINING:

5.2.1 Strategic Planning and land rights issues

The Minister is quite interested in triggering an ambitious program to help main cities to rapidly update or formulate their strategic plan and to improve the provision of public services. In this regard, there is the need to pass a government decree, already being prepared by the Ministry, suspending the old methodology. There is the opportunity to team up with the Ministry and the PRR (CSC) - SERAP group to start up an ambitious program of strengthening municipal management.

In this regard there is a cross-cutting problem affecting municipal development that requires special attention. Land ownership and legal rights have become a severe obstacle for planning and especially for housing development. Assistance is needed to solve in a practical way the illegal occupancy of public or private lands by persons representing economic interests, common people and even some government agencies.

5.2.2 Increasing municipality's own revenues

Notwithstanding central government interference, municipalities have a pretty well established tax structures capable of producing more revenues. This could be done by adjusting tax administration norms, strengthening procedures and instruments for determination, collection and enforcement of revenues. Increasing tax collection should go together with extensive utilization of user charges and fees as the provision of public services expands. These two efforts fully complement the possibility of accessing budget resources through the grant system proposed by the government in the FMPE law.

5.2.3 Budgeting adjustments.

This is a well developed area where there is not much to be done besides helping municipalities with TA&T to enhance their capability to design, formulate, implement and control specific projects. This will be complemented with assistance to ensure a strong link between planning and budgeting processes.

5.2.4 Public Services rationalization.

Municipalities should participate more actively in the provision of public services. In some cases scale economies, technical complexity and administrative benefits recommend the direct provision of the service. However, there is a vast camp of successful experiences with private-public joint ventures that deserve to be fully explored. There are already ongoing experiences with garbage collection in urban districts, primary health attention and street construction that could become interesting alternatives to direct provision by the municipalities.

6.0 LESSONS LEARNED

As high ranking officials in Kabul repeatedly stated in each of the interviews Afghanistan is a unitary state with a highly centralized political, fiscal and administrative government. This is unquestionably true; under the present institutional framework sub-national administrations -provinces and districts- are merely operative units that do not have their own resources or authority over expenditures. In this context, there is barely anything to be done in relation to Financial Management at this level of the administration.

However, things are moving quite fast in the political, legal and administrative scenario. As established in the Constitution within the principle of centralism, it is possible to transfer necessary powers to local administrations in order to accelerate and improve economic and social as well as cultural matters...” (article 137). The same Constitution created the provincial councils to help attain the objectives of the State as well as to improve provincial affairs. It also created the district councils to organize activities as well as the active participation of community in local affairs (138,139 and 140).

On the other hand, the government is moving forward with its efforts to modernize the provincial and district administrations, turning them toward development matters and to the attention to local basic needs. The process is well underway in Bakh, Samangan, Saripul, Jawzjan and Fariab as well as in Kabul and in their respective districts. But more than anything else, this is a political process with growing expectations all over the country climaxing on September 18 with the election of the Provincial Councils.

Delegating authority and resources has never been a linear process. From time to time, it has to circumvent obstacles or to face fundamental issues in order to be sustainable through time. Sound intentions are not free from risks or great challenges. In this regard, this report derives the following ten assistance projects from the GoA efforts to improve the living conditions of its population by enhancing the financial and administrative capability of the sub-national administrations. These ten projects either attempt to consolidate current efforts to build an effective and efficient central government or to support the attempts to enhance the financial capability of the sub-national administration in order to manage public resources (See Action Plan).

- **Enhance District’s capability to collect, plan and manage own resources.**

The purpose of this activity is to present districts with simple technical and managerial tools that allow them to start a collective process which includes participatory planning, effective tax collection -land and small shop taxes- and the application of these resources towards the objectives agreed upon with the local community. Government has to be consulted in relation to the transfer of tax revenue to districts. If government approval is not granted the project will focus on the elements to improve tax collection. A negative decision will greatly affect the intended results.

- **Improve Provincial Government capability to directly access Development Budget resources.**

The objective here is to enable the Governor’s Office with the technical and financial capabilities to design, formulate, manage, monitor and evaluate mid-size projects so they will meet recognized standards and become eligible for national or international funding. As capabilities and conditions differ significantly between provinces, this activity demands a close interaction with the ASP given its capacity to help balancing these differences, as well as with the PRR program in charge of the ongoing reforms.

- **Strengthening provincial municipality’s institutions and instruments to provide more and better local public goods and services.**

Provincial municipalities play an important role in the attention to basic needs. Municipalities have legally established responsibilities, their own resources and budget autonomy to carry out . The intention is to

modernize and make more effective the planning, financial and management tools and instruments employed by the municipalities enabling them to mobilize more resources to attend to the pressing needs of the local community. Here, the plan is to join efforts with the Ministry of Urban Development and Housing and the PRR-SERAP project to work with provincial municipalities on a voluntary basis.

- **Review the Financial Management and Expenditure Law and present options to enhance the role of sub-national administrations in the provision of local public goods.**

The FNPE law proposed by the government certainly provides a sound framework for the financial management of the central government. In doing so, it favors the financial aspects of the budget -to the detriment of other budget functions and the sub-national administrations. The idea of this activity is to elaborate and discuss with the government options that provide for functions such as monitoring and evaluation of results as well as proper support for sub-national administrations.

- **Ensure the effective participation and contribution of the Parliament in approving, executing and controlling the budget.**

The objective here is to provide MP with the technical tools and international experiences required to perform their functions, especially the fiscal and political control of budget results. In this regard it is advisable to extend this program with the proper adjustments to members of the Provincial Councils.

- **Provide the institutional elements and technical instruments and mechanisms to improve the accountability of the use of public resources.**

Initially this project will focus on improving the accountability for budget results within government agencies. Later as the system is consolidated, the system will be extended to the Parliament and will be made accessible to the general public. It is based upon establishing explicit results for programs and projects in the budget and a system of indicators to follow up on outputs and results.

- **Review operational and maintenance costs for critical ministries and propose its financing, internal or external, within a performance framework.**

Critical ministries such as education, agriculture and public works have an installed capacity which is underutilized. Greater output and better quality could be attained if schools were well supplied, teachers trained and extensionists able to fulfill their duties. It would be of great impact if those needs could be technically evaluated and resources ensured against explicit results in each of the chosen agencies. This program complements the effort to increase the accountability previously mentioned.

- **Improve the technical capability of line ministries and their provincial departments to formulate, monitor and evaluate projects financed either with their own resources or through donors' support.**

Despite efforts of the MoF to broadly extend the methodology and standards of the development budget, some of the ministries are lagging behind, thereby missing the opportunity to access those funds. The objective is basically to provide equal opportunities for all ministries to compete for national and international funding.

- **Increase transparency of decisions by government and donors in relation to the funding of projects and programs in the development budget.**

Criteria for selecting and assigning funds to projects are not clear or, at least, they are not well explained to competing agencies and officials. The need for transparency demands that the reasons for decisions and their results and costs be evident and accessible to the scrutiny of interested people and the general public. Here the objective is to establish the mechanisms to evaluate the criteria and standards employed in the decisions,

to evaluate both of them and to make the results obtained public. This mechanism will be extended to cover donors' decisions.

- **Improve the collection of tax revenues at the provincial level and establish a sharing formula so provinces participate in the increase in revenues.**

Despite efforts, revenue collection is lagging behind mid-term goals. One way to increase revenues and gain acceptance for new tax measures is to commit provincial governments to the endeavor and allow them to share in the value added. The purpose here is to provide TA&T for the tax administration reform stated in the Five Year Plan under the condition to discuss participation by provinces. As the government splits the tax management function from the Mustofiat, there is the need to provide TA&T to reinforce the remaining budget-expenditure function.

APPENDIX A PROPOSED SUB-NATIONAL FINANCIAL MANAGEMENT ACTION PLAN

The following draft Action Plan (AP) contains the set of strategic activities that might be carried out by ALGAP in order to enhance the capability of sub-national administrations to attend to the basic needs of the population of Afghanistan. The activities included seek to address institutional weakness identified in relation to planning, executing and controlling the budget as well as improving the performance of these organizations by enhancing the knowledge and skills of their staff. It will likely be beyond the capacity of ALGAP to pursue all of the activities outlined below, however it will be useful to develop a menu of technical assistance and capacity building options which may be used selectively depending on need and opportunity in selected Provinces and districts.

The AP includes five activity clusters that cover all levels of public administration in Afghanistan, from the district level to the political bodies (Parliament and Provincial Councils) and up to the law that provides the legal framework for Financial Management in Afghanistan—the Financial Management and Public Expenditure Law (FMPEL).

The AP starts by strengthening the capability of Districts to collect taxes, and to plan and manage them in order to partially attend to the basic needs of the local community. It also seeks to enable provincial governments with the technical and managerial tools to directly access donors' funds and the development budget. The AP presents provincial municipalities with the opportunity to modernize their planning, tax administration, budget programming and public service management tools in order to mobilize more resources and to apply them more efficiently to the provision of public goods and services.

Parliamentary examination and approval of the budget is a critical contribution for improving public resource assignments as well as for greater government credibility among citizens. The AP contemplates the provision of technical elements, material and experiences for MP and Provincial Councilors so they can carry on with the evaluation and political control of the budget. Finally, the AP includes the review of the FMPEL and the elaboration of some options that allow, not only for the consolidation of central government finances, but also for a further delegation of responsibilities to sub-national administrations.

Each of the projects included in the AP presents an objective, rationale and content, plus the resources and timeframe for its elaboration and implementation. It also presents potential risks that may affect its results or even its implementation. Finally, each project includes Jamal Nasir's responsibilities and Eduardo Fernandez's supportive contributions (For details see Manager Chart 1).

AP will follow up on the other five projects, leaving all doors open to work with them as soon as their conditions allow it.

Activity Cluster 1

Objective: Enhance district's capability to collect, plan and manage their own resources with community participation.

Rationale and Content:

The government of Afghanistan is making an effective presence with building new administration in over 140 districts. This project will complement the above activity and ensure that districts will be able to provide better services to the local community thereby increasing their confidence in the government of Afghanistan.

This activity presents districts with simple technical and managerial tools that allow them to start a collective process which includes participatory planning, effective tax collection —land and small shop taxes— and the application of these resources towards the objectives agreed upon with the local community. Later on districts might get together and elaborate projects and present them to donors or provincial government.

Approach:

The project will start by identifying institutional and organizational insufficiencies in the districts. This will be done with the help of a questionnaire that will be applied to a sample of districts located in the provinces of Kabul, Nangahar and Balkh. Then, the project will elaborate new or adjust old procedures for financial management and technical assistance and training to correct the insufficiencies and lack of knowledge and skills detected from the sample. Well known experts will design the material, modules and logistics to implement and provide technical assistance and trainings to the targeted districts.

There will be a special module for monitoring and evaluating which will be applied at the beginning of the project during the implementation and some time after the implementation is complete in order establish the impact of the project.

Resources and Time:

ALGAP will provide the technical and financial resources required for this project. The project requires the hiring of 3 local experts to work on participatory planning, tax management and accounting/reporting for one month. The project also considers the need to hire training experts to help with the design of the training module and to implement the technical assistance and training.

The project will last from 10/7/05 to 26/4/06

Opportunities and Risks:

For the project to work properly, a legal reform is needed to allow districts to spend the resources that they collect from local taxes. The MoF is nowadays trying to reestablish the land tax presenting the opportunity to introduce the recommended changes. If the government does not agree with the proposal to allow the districts to keep the revenues then there will not be incentives for the districts to collect those taxes, therefore reducing the likelihood for a successful and comprehensive project. Security is a constant problem that will affect the coverage of the all projects.

Jamal Nasir's responsibilities:

Jamal will be the coordinator of this project and his main functions will be the following:

- Select the specific districts for the sample, apply the questionnaire and present a report with the results and recommendations.
- Contact the local experts, prepare the TOR for the consultants and audit and approve their products.
- Help find the training experts and coordinate the elaboration of the modules and the training strategy with them.
- Coordinate and supervise the implementation, monitoring and evaluation of the training.

Eduardo Fernandez's support:

- Provide contacts and guidelines for Jamal's work, review TOR and documents and help to design new procedures and implementation process.
- Follow up the process at the time of implementation and provide guidelines for its evaluation.
- Review consultant's documents and help elaborate final recommendations.

Activity Cluster 2.

Objective: **Improve Provincial Government capability to directly access Development Budget resources.**

Rationale and Content:

PRR is moving forward with its administrative reform of provincial and district governments. The main purposes are to review the governors' functions, eliminate duplications, establish work flows and change operational procedures, job descriptions and staff requirements. Appointments will be based upon merit and open competition. The reform does not address financial issues which may become a source of frustration and loss of credibility in central government intervention.

The project seeks to provide the governors' offices with the technical and financial capabilities to design, formulate, manage, monitor and evaluate mid-size projects so they will meet recognized standards and become eligible for national or international funding.

Approach:

Two main issues limit the implementation of this project. On ~~the~~ one hand, there is the big capability "gap" among provinces which demands a differential approach according to the "development" grade of the provinces. On the other, there are some uncertainties about the coverage, pace and timetable for PRR's further reforms which deter ALGAP's interventions. In relation to the first point, it will be useful to learn from ASP's experience and to reinforce its technical and administrative capacity, in particular its presence in provinces grade 2 and 3. Here a cross cutting consultative group would be in charge of elaborating and presenting technically and financially sound projects to improve social service provision in second and third grade provinces. Either this or some variation of this type of intervention will help eliminate provincial isolation from the development budget and will certainly help ~~to~~ reduce regional inequities. This takes us to the second point. In provinces grade 1 assistance will be targeted on the technical services division created under the PRR's reform; therefore its existence is critical for deploying the required assistance. In the formulation of projects, a close collaboration with the respective sectoral department is expected.

In this regard, the project will keep preparing the strategy and needed material and training human resources. ALGAP will be in close touch with PRR and ASP to establish a definitive operation mode and time schedule.

Resources and Time frame:

The project requires experts on project formulation, design and evaluation. In this regard, it is important to have full cooperation from the Development Budget Office in the MoF in order to be able to access their methodologies. Depending on the pace of reforms, two financial management experts will also be needed to design a project management system and to implement it in provinces grade 1. Though the project is scheduled to start in August, 2005, its implementation begins in February, 2006 and continues until April, 2006. In this sense it provides latitude to adjust according to changing conditions.

Opportunities and Risks:

Balkh is already in stage 3 and the four surrounding provinces are in stage 2 with Kabul. Balkh will have its technical division ready by the end of August and the others in October. This is basically what is going on in terms of reform of subnational entities. Main risk is the discontinuity of PRR's efforts which will reduce the scope of the project and its impact.

Jamal Nasir's responsibilities:

- Keep in close contact with the people responsible for the PRR program and will report continuously on its advances. (See latest document on the Provincial Development Council)
- Start needs assessment of the two different types of provinces which includes going to Balkh and its surrounding provinces and work on Kabul where the PRR has already been made and write a report on these findings.
- Discuss with ASP the idea about a special team(s) for provinces grade 2 and 3.
- Prepare the TOR for the experts
- Supervise their work in the provinces

If all the conditions (PRR) are moving along smoothly then the project will be reignited along the lines above.

Eduardo Fernandez's support:

- Provide guidelines for the evaluation of provincial capabilities.
- Help to prepare the terms of reference for the local experts.
- Review experts' recommendations and help prepare final adjustments.
- Follow up the implementation process and provide guidelines for its evaluation.

Activity Cluster 3.

Objective: Strengthening provincial municipality's institutions and instruments to provide more and better local public goods and services

Rationale and Content:

Provincial municipalities play an important role in the provision of public goods and services. Municipalities have legally established responsibilities, their own resources and budget autonomy to attend to basic needs from local water supply and sewage up to housing and social and cultural urban amenities. Their performance varies greatly depending on their access to national resources and their management capability, but generally it is explained by their dependence on the central government and its Master Plan model.

The intention is to break away from this extremely complex and improbable Master Plan model into a strategic scheme that includes a vision of the municipality in the near future, a mission to be carried out in the context of pressing needs and possibilities within a regional and environmental perspective. This means devolving to the municipality some of the functions which, in the past, were assumed by the central government as well as strengthening their financial and administrative capabilities. It also considers an active role for local communities, particularly in their capacity to hold local authorities accountable for results.

The project seeks to modernize and make more effective the planning, tax administration, and financial and management procedures and instruments employed by the municipalities. Then municipalities will be able to mobilize more resources and to use them more efficiently to attend to the pressing needs of the local community.

Approach:

The project considers a joint effort with the Ministry of Urban Development and Housing and the PRR-SERAP project to work with provincial municipalities on a voluntary basis. Once a municipality shows an interest in participating in the program by signing an MOU, the project elaborates a diagnosis of present institutional conditions and organizational capabilities to continue with its planning and fiscal and financial function. Based on this initial review a group of experts on strategic planning, tax administration, budget

management and public service administration will establish, with the help of municipal officials, a comprehensive reform package to be implemented in the municipality. Hopefully, central government will provide budget resources —grants— to municipalities as established in the FMPE in reference to this type of efforts.

Resources and Time frame:

The project contemplates a division of labor where PRR will lead the administrative reform and the strategic planning and public service component and ALGAP will be in charge of fiscal and financial matters. The project contemplates hiring four experts, one each in strategic planning, public service management, tax management and budget and project management by ALGAP and PRR according to their responsibilities.

The time span for this project extends from September, 2005, to July, 2006, though implementation will start in March, 2006.

Opportunities and Risks:

Minister of Urban Development and the mayors of Herat and Massar I Shariff showed interested in the project. As it was mentioned PRR is working in the Kabul and hopes to expand the model to other cities. This is a complex project that demands close collaboration with the PRR-IARCSC program as well as with the Ministry of Urban Development and Housing not to mention the participation of the municipality's staff and top ranking officials. Lack of any of these elements will jeopardize the project's expected outcomes.

Jamal Nasir's responsibilities:

Participate in the identification of the needs of municipalities that show interest in participating in this program. Write a report on initial findings.

Keep inform the COP about the evolution of this project and the resources needed from ALGAP for its implementation.

Coordinate the implementation of the project.

Eduardo Fernandez's support:

Direct the process of identification of municipalities' needs and write a report on findings.

Promote the formation of a multi organizational group and help consolidate this project by establishing the components and the responsibilities and commitments of different partners.

Participate with the other partners in the elaboration of terms of reference for the experts.

Participate and help to coordinate the work of experts and review final documents.

Participate actively during the implementation of the project.

Prepare guidelines for the evaluation of the project.

Activity Cluster 4.

Objective: Review the Financial Management and Expenditure Law and present options to enhance the role of subnational administrations in the provision of local public goods.

Rationale and Content:

The FNPE law proposed by the government certainly provides a sound framework for the financial management of the central government. It is a well designed law that meets international standards. Nonetheless there are some elements that deserve further discussion, especially in relation to the following:

the lack of transparency for programming and assigning resources within the development budget, the inadequate treatment granted to intergovernmental fiscal relations, the inappropriateness of the Mustofiat to manage them, the lack of technical instruments to establish budget outputs, to follow up them and to hold officials accountable.

Among other things, the law should provide greater equality and accessibility to the Development Budget, introduce instruments and mechanisms to monitor and evaluate budget results and provide proper consideration for sub-national fiscal and financial issues.

Approach:

The idea is to elaborate a document that gathers the aforementioned issues as well as other concerns from interested parties. The document should be discussed with the MoF, made public and discussed in academic and political encounters.

Resources and Time frame:

It requires hiring a local expert for two months. This expert should be related to the University and/ or AREU.

Risks:

The unwillingness of the MoF to discuss the issue

Jamal Nasir's responsibilities:

To coordinate the elaboration of the documents and seminars.

Eduardo Fernandez's support:

To comment and provide inputs on the documents

Activity Cluster 5.

Objective: Ensure the effective participation and contribution of the Parliament in approving, executing and controlling the budget.

Rationale and Content:

Altogether the limited role in budget preparation assigned by the Constitution and the prevailing fiscal conditions in Afghanistan will disconcert most of elected MP next September. There is the risk that disenchantment with budget figures and fiscal issues might result in its disengagement from fiscal and financial management issues or in an endless political feud too costly for the country.

This project is expected to lessen this risk by:

- Building up MP's capacity to deal with fiscal and financial affairs and expose them to similar experiences in other countries.
- Providing the Parliament with accurate, appropriate and timely information as well as with documentary explanation of tax and spending proposals.
- Defining expected outputs and results for programs and projects in the budget and, in this way, facilitate the understanding of government policies and their adequate control.
- Establishing a small technical unit able to monitor and evaluate strategic programs during their execution.

Approach:

The objective here is to provide MP with knowledge, technical tools and international experiences required to perform their functions, especially the fiscal and political control of the budget. In this regard it is advisable to extend this program with the proper adjustments to members of the Provincial Councils

Resources and Time frame:

Contact local experts to prepare the seminar. The time frame will be from October, 2005 until May, 2006.

Risks:

Jamal Nasir's responsibilities:

Coordinate the preparations for the seminars and study tours

Eduardo Fernandez's support:

Help in preparing the materials and securing contacts for the seminars

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