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REPUBLIC OF SENEGAL
PARTICIPATORY LOCAL DEVELOPMENT PROGRAM (PLDP)
DRAFT FINANCIAL MANAGEMENT ASSESSMENT (FMA)

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1. INTRODUCTION

Two CDD projects (National Rural Infrastructure Project and Social Development Project), which were initially designed as Adaptable Program Lending, were successful in achieving their respective development objectives. During the preparation of their second phase, the government has expressed its desire to consolidate its decentralization and local development portfolio. In that regard, a national local participatory development program was proposed and all donors including the Bank were invited to finance. This was an excellent opportunity for the Bank because the Country team was discussing the possibility of consolidating the portfolio and harmonizing the intervention at the local level.

In the end, financing one consolidated project was preferred as it is in order with both the government's and the Bank's strategic orientations.

As part of the preparation of the project, a financial management assessment was conducted to determine whether the implementing entities (a Project Coordination Unit at the central level, the ARD¹ at the regional level and the local representative of the Treasury department at the local level), in charge of the implementation of the project have acceptable financial management arrangements. This report presents the conclusions of the financial management assessment.

2. EXECUTIVE SUMMARY AND CONCLUSION

The Country Financial Management Assessment (CFAA) of Senegal was conducted in 2003. The table in annex 1 shows the Financial Management Risk Assessment at the Country level. The overall risk rating of the public financial management system was high. Since that exercise, the Government has created an executive secretariat under the Ministry of economy and finance to monitor the implementation of the action plan of the CFAA. The recent HIPC Country Assessment and Action Plan by the Bank and the IMF in November 2004 showed important improvements in the areas of public expenditure tracking – notably in the priority areas defined in the PRSP, internal controls, and budget preparation. However, significant progress is still needed in internal and external controls of budget execution and state-owned enterprises.

In addition, no progress was made on decentralization and local government finance. Various studies in Senegal show that excessive centralization of decision-making and lacks of accountability undermine community and local governments' ability to manage their own affairs. Inadequate fiscal intergovernmental fiscal transfers, cumbersome procedures, and a weak system for tax collection also seriously hamper local development. The National Rural Infrastructure Project during its first phase has assisted in addressing some of the deficiencies notably institutional capacity and accountability and transparency. The PLDP project will leverage on the financial management arrangements of the National Rural Infrastructure Project at the local level. Fiduciary Management activities at the local level will be carried out using existing local public financial management procedures.

¹ Agences Régionales de Développement

A financial management assessment was carried out to determine whether the implementing entities (the Project Coordination Unit at the central level, the ARD² at the regional level and the local representative of the Treasury department at the local level), in charge of the implementation of the project have acceptable financial management arrangements.

The conclusion of the assessment is that the financial management arrangements for the project need to be improved before project effectiveness to satisfy the Bank's minimum requirements under OP/BP10.02 and will then be adequate to provide, with reasonable assurance, accurate and timely information on the status of the project required by IDA. The financial management arrangements will be strengthened with the implementation of the action plan in annex 1.

3. SUMMARY OF THE PROJECT DESIGN

The project development objective is to promote the full use of community-driven development strategy for poverty alleviation by encouraging the involvement of all sectors, Rural Communities and beneficiary communities in the provision of quality basic social and economic services to the poorest populations.

The Local Participatory Development Project would be implemented through three (3) operational components:

- (i) Support to national government to develop a national CDD framework;
- (ii) Local Investment Fund and,
- (iii) Capacity-building program for local development.

In addition, a Coordination component will be set up comprising Project Management, Communication, and Monitoring and Evaluation.

4. ASSESSEMENT OF THE RISKS

4.1 AT THE COUNTRY LEVEL

The Country Financial Management Assessment (CFAA) of Senegal was conducted in 2003. The table in annex 3 shows the Financial Management Risk Assessment at the Country level. The overall risk rating of the public financial management system was high. Since that exercise, the Government has created an executive secretariat under the Ministry of economy and finance to monitor the implementation of the action plan of the CFAA. The recent HIPC Country Assessment and Action Plan by the Bank and the IMF in November 2004 showed important improvements in the areas of public expenditure tracking – notably in the priority areas defined in the PRSP, internal controls, and budget preparation. However, significant progress is still needed in internal and external controls of budget execution and state-owned enterprises.

The government has given priority to improvements in these areas as well as local governance finance reforms. A Multi Donor Trust Fund (MDTF) to follow up the

² Agences Régionales de Développement

implementation of the reforms was set up. An IDF Grant to strengthen the capacity of the Supreme Audit Institution ("Cour des Comptes") is also under implementation. The PLDP project will leverage on the achievements of the IDF as well as the other assistance of the donors to "Cour des Comptes". This institution will then be involved in the audit of Rural Communities.

4.2 AT THE PROJECT LEVEL

Because of the high fiduciary risk at the country level, IDA has taken special measures to ensure adequate financial management of its portfolio. Project management staffs are appointed on a competitive basis and Bank funding is following special mechanisms to mitigate fiduciary risk. IDA projects are invariably audited by independent and competent auditing firms. However, the PLDP project will leverage on the achievements of the National Rural Infrastructure Project at the local level and will use the country systems at that level. Moreover and given the on going capacity building program of the Bank and the donors, "Cour des Comptes" will be involved in the audit of the Rural Communities.

5. INSTITUTIONAL ARRANGEMENTS

The charts in annex 2 give an overview of the project's institutional arrangements.

Overall project orientation and coordination.

The overall project orientation will be the responsibility of a Steering Committee (SC), set up by the government to coordinate the implementation of its CDD framework. The Coordination authority will be headed by the Office of the Prime Minister and will include high-level representatives from all key line ministries, the Local Governments' Association (AEL), the private sector, and the donor community. Its mandate includes: (i) developing, adopting, monitoring and evaluating the national CDD framework; (ii) coordinating the implementation of the national CDD framework while leaving the implementation to the partners (ministries, Local Governments and Rural Communities).

Project Coordination and implementation.

At the national level

A Project Coordination Unit (PCU) will be set up at the national level to oversee and coordinate the day-to-day implementation of project activities. The PCU will coordinate and consolidate annual work plans and budgets and oversee the financial management, procurement and monitoring and evaluation of activities and feed the results into the national poverty monitoring system.

The PCU will be made of a Project Coordinator, a Financial Management Specialist, a Monitoring and Evaluation Specialist, a Procurement Specialist and an Operation Officer. The annex 2-1 shows the organizational chart of the PCU.

At the Regional level

The implementation of the project will be supervised at the regional by the ARDs. During the pre-appraisal mission, an assessment of ARDs stressed out the need to (i) review their mandate and legal texts, (ii) staff ARD with qualified and experienced professionals to handle the project. Key staff or ARDs to be recruited on a competitive

basis prior to Credit's effectiveness will include: the Director of ARD, the Financial Management Specialist, the M&E Specialist, the Infrastructure Specialist, the Micro Projects Specialist, the Procurement Specialist (see the new organizational chart of ARD in annex 2-1).

At the local level

At the local level, the project will be implemented by the Rural Communities (RCs) and local representatives of the Treasury Department: Rural Collectors. Rural Collectors will be responsible for identifying and implementing community infrastructure projects. This will be done on a participatory basis and with the assistance of the ARDs.

6. FINANCIAL MANAGEMENT AND DISBURSEMENT ARRANGEMENTS

6.1 Financial Management Arrangements

Staffing arrangements

At the national level, the Financial Management (FM) system of the project will be coordinated by a Financial Management Specialist assisted by an Accountant whereas the FM specialist of the ARD will handle the FM system at the regional level.

This FM staff, with experience and qualifications satisfactory to IDA will be recruited prior to Credit's effectiveness.

The FM team at the national level will report periodically to the Director the Debt and Investment (DDI) in Senegal.

As far as financial management is concerned, they will have the responsibility (i) to collect and control invoices, (ii) keep and maintain the books, (iii) enter data in the accounting software, (iv) monitor the special account which, according to the national institutional arrangements in Senegal, is managed by DDI, (v) prepare the Financial Monitoring Reports (FMR) as well as the annual financial statements, (vi) ensure that annual audits are done.

At the regional level, the FM specialist of the ARD will have the responsibility to collect relevant information from Rural Collectors and maintain the information system. They will also provide the relevant input for the FMR.

At the Rural level, Rural Collectors will have the responsibility of maintaining the accounts, collecting and controlling invoices, keeping the books, providing all the accounting information to the FM specialist of ARD and paying suppliers or NGO/CBO following the Agreement between the Project and the Treasury Department.

Accounting Policies and Procedures

The PCU will apply the existing private accounting system in Senegal (SYSCOA) issued in 1998. This system is based on the *Plan Comptable* traditional in French-speaking

countries, with several innovations mirroring some principles set in International Accounting Standards. The SYSCOA has a three-tier structure (full reporting basis; simplified basis; cash basis). The PCU will be eligible for the simplified system. Moreover, the project will leverage on the first phase of the NRIP and the disbursement method will be the FMR based disbursement mechanism. Prior to Credit's effectiveness, a manual will be developed and will provide all the required details on administrative, accounting and financial procedures. This manual will be an update of the NRIP and the Social Development Fund manuals.

Accounting Software

The project will use the existing accounting software of the NRIP at the national and regional level. The existing accounting software will be customized to fit with then new component and activities of the project.

Reporting and Monitoring

The project will use the FMR-based disbursement mechanism and will prepare and furnish to the World Bank a Financial Monitoring Report (FMR), in form and substance satisfactory to the World Bank, which:

- (i) sets forth sources and uses of funds for the project, both cumulatively and for the period covered by said report, showing separately funds provided under the Credit, and explains variances between the actual and planned uses of such funds;
- (ii) describes physical progress in project implementation, both cumulatively and for the period covered by said report, and explains variances between the actual and planned Project implementation; and
- (iii) sets forth the status of procurement under the project, as at the end of the period covered by said report.

The first FMR shall be furnished to the World Bank not later than 45 days after the end of the first calendar quarter after the Effective Date, and shall cover the period from the incurrence of the first expenditure under the project through the end of such first calendar quarter; thereafter, each FMR shall be furnished to the World Bank not later than 45 days after each subsequent calendar quarter, and shall cover such calendar quarter.

Formats and contents of the FMRs will be defined and agreed during the appraisal mission and confirmed during negotiations.

The PCU will also be required to produce, not later than June 30 of the following fiscal year, audited annual financial statements following the simplified system of SYSCOA. These financial statements will be subject to periodic audits (see paragraph on audits).

Internal Audit

At the national level, internal audit function in Senegal is carried out by the Director of the Debt and Investment (DDI) department. This function consists of controlling ex ante all the expenditures supporting documents and withdrawal applications before sending them to the Bank. This is not a satisfactory internal audit arrangement and does not provide the assurance of the continuing adequacy of and conformity of the PCU with the project's procedures.

The Bank will therefore pay a particular attention to this internal control during supervision missions.

External Audit

Annual audits of the Project's financial statements

External auditors with qualifications and experience satisfactory to the World Bank will conduct an annual audit of the project's financial statements. This audit should be carried out in accordance with International Standards on Auditing (ISA), and will include such tests and controls as the auditor considers necessary under the circumstances.

The selection process of the auditors will be done in coordination with the Supreme Audit Institution in Senegal i.e. "Cour des Comptes".

"Cour des Comptes" will prepare the Request For Proposals of the auditors, chair the selection committee and assess the auditor's performance.

The Bank will finance the audit costs and only one opinion on the financial statements will be required.

Annual Audits of the Rural Communities

During its first phase, the project will strengthen the capacity of "Cour des Comptes" to handle regular audits of Local Governments.

In the mean time, "Cour des Comptes" will select private auditing firms with experience and qualifications satisfactory to IDA to conduct annual audits of Rural Communities.

The first audits of RC will be done after two years of implementation of the project.

The tables bellow summarized the auditing requirements under this project:

Audit report	Entity	Due Date
1) Project's financial statements	PCU	June 30
2) Annual Audits of the Rural Communities	Rural Communities	June 30, 2008(*)

All the audit reports will be submitted to the Bank within six months after year end (12/31/n).

(*) if the project is effective in 2006, the first annual audits of the RC will be the 2007 accounts.

Flow of funds

The chart in annex 4 presents the flow of funds and information of the project.

There would be two accounts at the national level:

- the special account managed by DDI,
- the Treasury account managed by the Treasury Department.

The Government funds will be channeled through the FECL³ and the FDD⁴

The donors are expecting to come to the Treasury account managed by the Treasury department.

³ Fonds d'Equipement des Collectivités Locales

⁴ Fonds de Dotation de la Décentralisation

The work program, the annual budget and the disbursement forecasts will be agreed annually between the Bank and the donors. Once it's agreed the Bank and the donors will release the quarterly needs from the Credit Account to the Special Account and then the Treasury Account. The Treasury department will then disburse the funds to Rural Collectors based on the Work Program of Rural Communities.

Each Rural Collector will open a specific account to follow up the use of funds of donors. Every month, Rural Collectors will report to the FMS of the ARD on the use of funds. The documents sent to the FMS of ARD will include a bank reconciliation statement, local bank statement, the financial report on the budget execution, forecasts for the next quarter. The FMS of ARD will then consolidate and transmit on a monthly basis that information to the PCU who will prepare the quarterly FMR.

Under the project, the Government will address the weaknesses of FECL and FDD identified by the assessment done during the preparation of the project.

6.2 Disbursement Arrangements

The project will not use the Statement Of Expenditures method of disbursement. All disbursements will be report (FMR) based. Before any withdrawal is made from the Credit Account, the PCU must submit to the Bank a FMR, a statement with the projected sources and applications of funds for the Project for the six-month period following the date of the request, and any other information requested by the Bank by notice. As stated above, the formats and contents of the FMRs will be defined and agreed during the appraisal mission and confirmed during negotiations.

Special Account

The special account of the project will be managed by the Director of Debt and Investment (DDI) department in the Ministry of Finance who is the main authorizer ("ordonnateur") of capital expenditures in Senegal.

Upon receipt of each application for withdrawal of an amount of the Credit, the Bank will, on behalf of the Borrower, withdraw from the Credit Account and deposit into the Special Account an amount equal to the lesser of: (a) the amount so requested; and (b) the amount which the Bank has determined, based on the reports (FMR and any other information requested by the Bank by notice) applicable to such withdrawal application, is required to be deposited in order to finance Eligible Expenditures during the six-month period following the date of such reports.

The special account will be used to finance eligible expenditures and transfer funds to the Treasury Department and the local accounts.

Treasury Account

An account will be opened at the central level in the Treasury department. This account will be used for the Local Investment Funds (LIF) of the Rural Communities. Funds will be channeled from this account directly to Rural Accounts managed by Rural Collectors. The LIF will be used to finance part of the Local development Plans (LDP). An Agreement between the Rural Community (RC) and the PCU will outline the specific items of the LDP to be financed under the project.

The project will provide small grants to community based and producer organizations for technical assistance in the design and for the implementation of productive, income

generating and natural resources management activities identified through participatory approaches, following key strategic local development objectives spelled out in the local development plans. This Treasury Account will be a basket funding and all the donors are expecting to contribute to the program via this account.

Rural Accounts

Rural Accounts will be opened by Rural Collectors and will be used to directly pay goods and services related to the RC Agreement. The annex 4-2 gives the details of the execution of the budget at the local level.

Counterpart Funding

As stated above, the Government will contribute mainly under the FECL and the FDD. The two funds will be increased as follow:

	FECL	FDD
2006	XX%	XX%
2007	XX%	XX%
2008	XX%	XX%

Category recap

	Categories	Credit Allocated in US\$	% of expenditures to be financed
(1)	Goods	3,600	100% of foreign expenditures and 90% of local expenditures
(2)	Consultants' services, Training and audits	18,800	100% of foreign expenditures and 90% of local expenditures
(3)	Subprojects	17,100	100%
(4)	Matching Grant for Income Generating Activity	7,600	100%
(5)	Operating costs	600	90%
(6)	Reimbursement of Project Preparation Facility (PPF)		Amount due pursuant to the relevant section of the DCA
(7)	Unallocated	2,300	
TOTAL		50,000	

7. LOAN CONDITIONS AND OTHER FINANCIAL COVENANTS

Negotiations conditions

The negotiations conditions are the following:

- the Borrower has recruited for the Project Coordination Unit a financial management specialist with experience and qualifications satisfactory to the Association;
- the Borrower has elaborated an administrative and accounting manual and installed at the PCU an accounting software.
- The Borrower has appointed an external auditor with qualifications and experience satisfactory to the Association.
- The Borrower has amended the decree of ARD to fit with its new mandate.

Effectiveness conditions

- The Borrower has appointed to each ARD: (i) a Director, (ii) a financial management specialist, (iii) a procurement specialist, (iv) a Monitoring and Evaluation Specialist, (v) an infrastructure specialist and a (vi) Micro Project Specialist, all having qualifications and experience satisfactory to the Association.

Counterpart Funding

- Distribute FDD and FECL transfers to local governments before March of the year,
- Increase the FDD and FECL as follow:

	FECL	FDD
2006	XX%	XX%
2007	XX%	XX%
2008	XX%	XX%

8. SUPERVISION PLAN

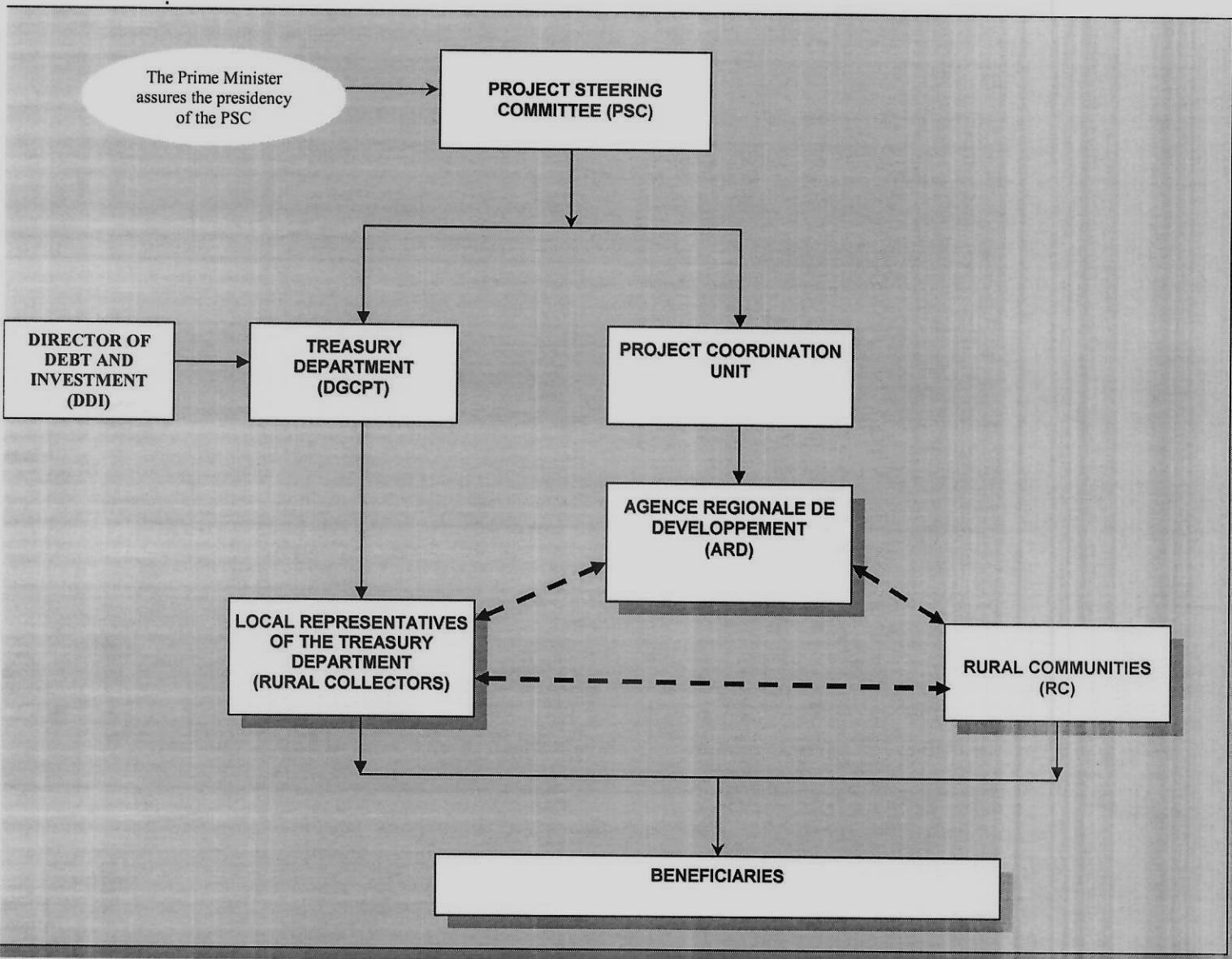
On a regular basis (at least once per year), the system will be reviewed and assessed. The FMRs will be reviewed as well as the audit reports.

Annex 1: Financial Management Action Plan

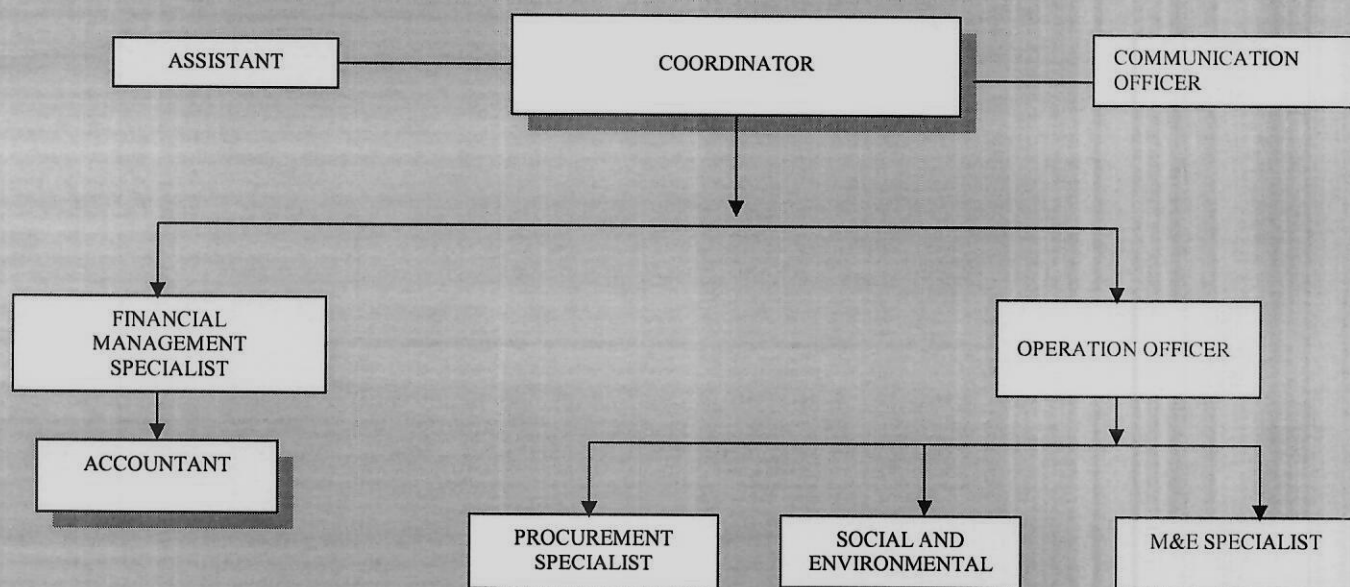
Action	Tasks	Entity	Target Completion Date
<u>Staffing</u>	<ul style="list-style-type: none"> ▪ Recruitment of the PCU staff ▪ Staffing of ARD 	<ul style="list-style-type: none"> ▪ Prime Minister ▪ Prime Minister 	<ul style="list-style-type: none"> ▪ Negotiations ▪ Effectiveness
<u>Administrative and Accounting Manual</u>	Updating the administrative and accounting manual including the agreement with the Treasury department	Preparation Team	Negotiations
<u>External Audit</u>	Recruitment of an auditor satisfactory to IDA <ul style="list-style-type: none"> ▪ Expression of interest ▪ Request for Non Objection on the RFP including the short list ▪ World Bank's non-objection on the request for proposals package ▪ Requests for proposals sent out ▪ Proposals received ▪ Technical evaluation completed and approved by IDA ▪ Financial evaluation completed and contract awarded and approved by IDA 	Preparation Team / IDA	Negotiations
<u>Accounting software</u>	<ul style="list-style-type: none"> ▪ Updating the accounting software satisfactory to IDA 	Preparation Team	Negotiations
<u>Counterpart Funds</u>	<ul style="list-style-type: none"> ▪ Annual needs of counterpart funds included in the budget of the state in the FECL and the FDD 	Ministry of Finance	First Quarter of the Year

Annex 2: Organizational Chart of the Project

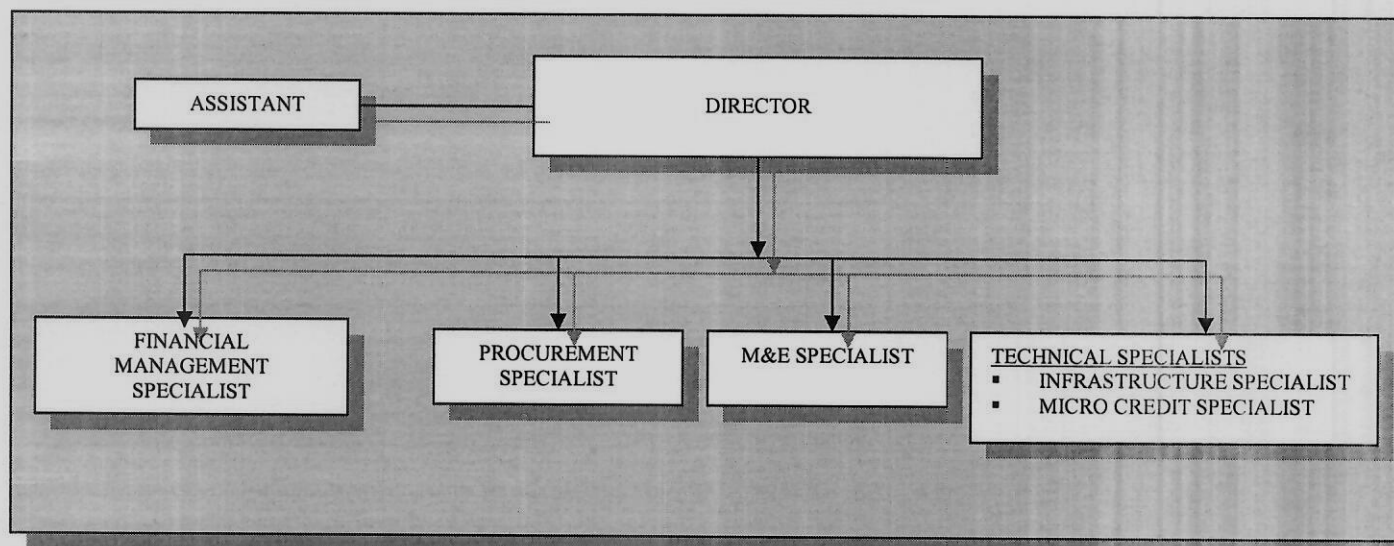
The overall set up of the Project is shown in the diagram below:



Annex 2-1: Organizational chart of the Project Coordination Unit



Annex 2-2: The organizational chart of the ARD is described bellow:

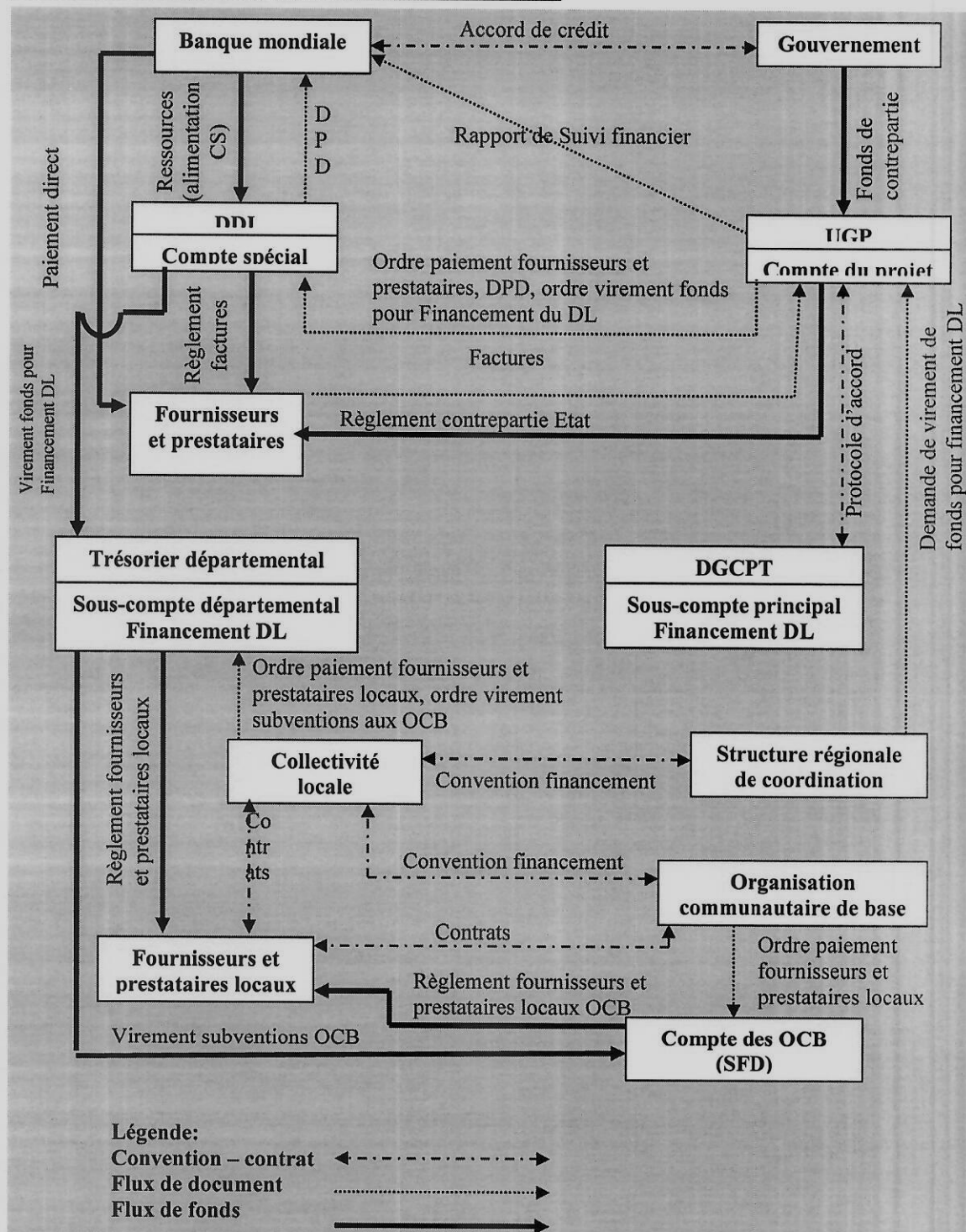


Annex 3: Risk Assessment and Internal Control

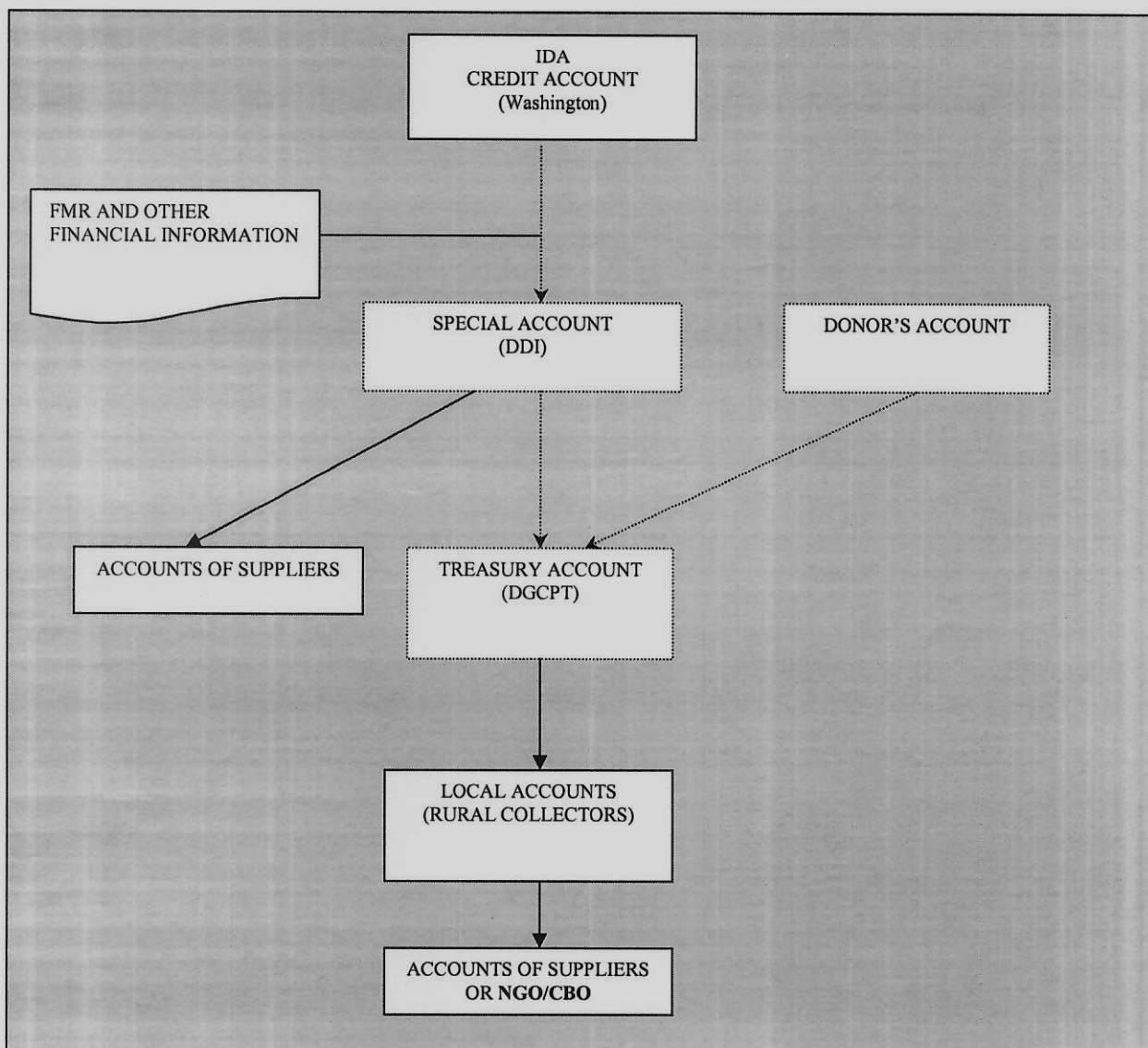
	Risk Assessment				
	H	M	L	N	Comments
Inherent Risk					
<i>Inherent risk is the susceptibility of the project financial management system to factors arising from the environment in which it operates, such as country rules and regulations and entity working environment (assuming absence of any counter checks or internal controls).</i>					
1. Corruption		X			The CFAA action plan is under implementation and the government has created an executive secretariat to follow up.
2. Poor governance		X			
3. Weak Judiciary		X			
4. Weak Management capacity		X			
Overall Rating Inherent Risk		X			
Control Risk					
<i>Control risk is the risk that the project's accounting and internal control framework are inadequate to ensure project funds are used economically and efficiently and for the purpose intended, and that the use of funds is properly reported.</i>					
1. Implementing Entity		X			Idem inherent risk
2. Funds Flow		X			
3. Counterpart funds <ul style="list-style-type: none">▪ Delay on adoption of the repartition law of the FECL and the FDD			X		<ul style="list-style-type: none">▪ This action is included in the PRSC matrix
4. Staffing <ul style="list-style-type: none">▪ Delay and political resistance on the staffing of the ARD			X		<p>The FMSs will be recruited under TORs acceptable to IDA</p> <ul style="list-style-type: none">▪ This action is an effectiveness condition
5. Accounting Policies and Procedures			X		The update of the manual is part of negotiation conditions
6. Internal Audit		X			The bank will pay attention to the internal control system during supervision mission
7. External Audit		X			Prior to Credit Effectiveness, an external auditor under TORs acceptable to IDA will be recruited
8. Reporting and Monitoring			X		The Bank will assist the PCU in defining the format of the quarterly reports
9. Information Systems			X		The existing accounting software of NRIP will be customized to the PLDP
Overall Control Risk		X			The action plan attached in annex 1 will be implemented prior to Credit negotiations

H: High M: Moderate L: low N/A: Not Applicable

Annex 4: Flow of Funds and Information



Annex 4-1: Report-Based Mechanism



Annex 4-2: Payment of goods or services at the Local Level

