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EOI 13/13 Review and assessment of national and sector policies in relation to budget support modalities in the Pacific Smaller Island States:

Sub-component to review and assess preconditions for projects through the Global Climate Change Alliance in the Pacific and SIDS regions using budget support modalities

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Eligibility and Preconditions for Climate Change Financing through Budget Support

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1 BACKGROUND

The consultant has been engaged to review the eligibility requirements for climate change finance through budget support, especially as required by the European Union (EU) and under the Global Climate Change Alliance (GCCA). The review is based upon a desktop analysis of available information provided through independent research and that collected by the national and sector policies review team[1]. The Terms of Reference are attached in Annex 1.

In 2007 the EU was pivotal in the establishment of the Global Climate Change Alliance (GCCA). The provision of financial support through budget support programs was envisaged at the onset as a potentially more effective way to channel funds for climate change activities[2].

The GCCA provides a program for dialogue at national, regional and global levels on practical ways in which to incorporate climate change policies, based on experiences into development policy and budgets. The second pillar is technical and financial support to countries for climate change activities. The focus of these activities is five priority areas:-

- Mainstreaming climate change into poverty reduction and development efforts
- Adaptation
- Reducing Emissions from Deforestation and Forest Degradation (REDD)
- Enhancing participation in the global carbon market
- Disaster Risk Reduction (DRR)

At the end of 2012 the GCCA had 45 ongoing programs in 35 countries spread over four regions[3]. It has a resource envelope of €285 mil of which €27 mil[4] has been provided in the form of Budget support programs. Three of these countries are Small Island Developing States (SIDS) and this report examines the background to these three SIDS that have received GCCA budget support.

2 REQUIREMENTS FOR BUDGET SUPPORT FINANCE THROUGH THE EUROPEAN UNION (EU)

2.1 CURRENT EC DIRECTIVES

Budget Support (BS) is a modality of support in which a donor is providing financial transfers directly to the Treasury of the recipient country. It is used as a means of delivering aid through partner government systems and thereby enhancing the capacity of these systems through its utilisation. It involves policy dialogue, a high degree of fiduciary accountability, partnership and mutual accountability. It has been a common form of development assistance used by multi-lateral donors in the past and is increasingly being used as part of bi-lateral assistance programs.

[1] P4SD, Matt Mcintryre; Christopher Cheatham and Francis Toomey

[2] Implementation framework of the global climate change alliance, Commission staff working document:, p.5, July 2008, Brussels, 15.7.2008 SEC(2008) 2319, EC

[3] Paving the Way for Climate Compatible Development: Experiences from the Global Climate Change Alliance, Global Climate Change Alliance, p.5, European Union, 2012

[4] *ibid*, From Table 1 Overview of GCCA funding

In 2010 the EU undertook a review of ten years' experience of budget support that it has provided to third countries[5]. The new policy for BS for the EU was launched in 2011 and it sets out the requirement for a country to meet underlying principles, to engage in policy dialogue as well as meeting eligibility criteria both when a BS program is considered and during implementation. The policy paper made special reference to the situation facing SIDS/OCT's and these have been reflected in the new guidelines[6]. Whilst this policy is similar to the earlier arrangements it is clear that some countries have qualified for BS under earlier arrangements.

The specific objectives of individual budget support programmes should be aligned with partner countries own development policies, priorities and objectives (and thus harmonised and coordinated with other aligned donors). They should also be consistent with EU development policy.

Since BS feeds directly into the fiscal budget of the recipient country there is a requirement for it to have predictability. Therefore the emphasis is on development strategies that are nationally owned and for the EU to use performance related tranches to provide transfers that can be related to results-based budget outcomes.

The current EU directives for considering BS as a modality for support require the country to meet the principles of EU development policy and the eligibility criteria.

2.2 PRINCIPLES OF EU DEVELOPMENT POLICY

The view of the EU is that BS forms contractual partnership which has the common objective between the EU and partner countries in order to build and consolidate democracies, pursue sustainable economic growth and eradicate poverty. The underlying principle is that there is a shared commitment to fundamental values of human rights, democracy and the rule of law.

Meeting this underlying principle is essential for the policy dialogue to commence in relation to BS. Since direct BS is seen as a form of endorsement of Government policy there has to be a high degree of trust that the recipient country will continue pursuing these fundamentals of EU policy. A secondary benefit through providing general BS is the improvement of domestic accountability and strengthening national control mechanisms as a basis for improving governance and adherence to fundamental values. Should countries that are receiving direct BS trend away from commitment to these principles (where there is a clear financial risk or the reputation of the EU may be damaged) the support can be suspended immediately -. In other cases there is a proportionate response.

There are three forms[7] of BS provided by the EU. *Good Governance and Development Contracts (GGDC)* are used whenever the specific objectives are focused on fostering domestic accountability and strengthening national control mechanisms or on strengthening core government systems and supporting broader reforms, such as macroeconomic management, public financial management (including procurement and the fight against corruption), domestic revenue mobilisation and public sector reform, and addressing constraints to sustained and inclusive growth. This is the main form of general budget support.

[5] The future approach to EU budget support to third countries - Communication From The Commission To The European Parliament, The Council, The European Economic And Social Committee and the Committee of the Regions, Brussels, 13.10.2011 COM(2011) 638 final, European Commission

[6] Budget Support Guidelines, Programming, Design and Management –A modern Approach to Budget Support, Annex 10, September 2012

[7] Ibid. p.13

Sector Reform Contracts (SRC). These are used when the specific objectives are more narrowly focused on supporting sector policies and reforms, improving governance and service delivery in a specific sector or set of interlinked sectors. When providing SRC, emphasis is placed on the equitable access to and quality of public service delivery, particularly to the poor, on the promotion of gender equality and children's rights. The capacity to absorb and use sector research results, as well as creating conditions at sector level for inclusive and sustainable growth are also areas of emphasis. Increased financial resources to a sector may be a feature of many SRC programmes; however they may also have objectives that do not necessarily imply significant increases in sector expenditure. The value added of a SRC is often in supporting an acceleration of reforms, in improving efficiency and effectiveness of sector expenditures, in knowledge sharing or capacity development.

The preferred focus is on sectors that encourage development and the reduction in poverty, in particular assistance that addresses basic population needs such as health, education, water and sanitation. Under sector support programs the financial assistance is targeted to within an individual sector of the recipient government's activities.

State Building Contracts (SBCs) are used when situations of fragility or transition require action to support transition processes towards development and democratic governance, including sustainable changes in transition societies, to help partner countries to ensure vital state functions and to deliver basic services to the populations. Assessments of eligibility for SBCs focus more on the forward looking political commitment and institutional reforms than backward looking track record, they require stronger political and policy dialogue and, if necessary, closer monitoring and possible targeting of EU funds.

The policy of the EU in relation to the provision of BS to a country is that it will be assessed on a case by case basis and will consider the potential benefits from direct financial support through government systems and the risks of providing assistance this way.

The EU policy acknowledges the structural vulnerability of SIDS, particularly in relation to Climate Change. In considering BS for SIDS it considers that there are four challenges that need to be considered as cross-cutting issues in SIDS BS. These are:-

Vulnerability: to natural disasters, economic or terms of trade shocks and aid volatility. High levels of debt that reduce the resilience capacity to shocks by SIDS; Reducing vulnerability to hazards through mitigation and adaptation is regarded as being critical and should be a key component of SIDS development strategies for a sustainable development. The negative impacts of climate change are regarded as increasing this vulnerability, which is acknowledged as disproportionally affecting SIDS along with pre-existing distance and energy constraints. The relationship between these effects and overall development goals (such as MDGs) is also acknowledged, outlining the close links between climate change adaptation and development strategies in SIDS.

Volatility: Small states have needed to overcome obstacles of scale by increasing trade and specializing in a small number of exports to a selected number of large markets, as well as in tourism. This reliance on specialization has increased vulnerability to rapid shifts in the terms of trade and changes in economic conditions in the world markets. They experience also greater volatility in growth. Combined with their vulnerability, this extreme volatility makes development planning particularly challenging in SIDS and the requirement is for strategies that take these uncertainties into account and builds in an element of flexibility.

Natural resources management: Tourism and natural resources play an important role in the growth experience of most strongly performing SIDS. The presence of natural resource wealth can be an opportunity for rapid growth and, therefore, for poverty eradication or for the achievement of sustainable development. Contests over ownership and access to natural resources have in some countries lead to conflict, corruption and ineffective governance. In that respect, building capacity for managing natural resource wealth its governance, and its environmental and social impact, are essential in SIDS.

Institutional Capacity: Many SIDS have very small administrations, weak institutional capacity and weak core state or local government functions. However, by comparison, public sector expenditures tend to be relatively high. Broad and generalized reform agendas are therefore regarded as being unlikely to be successful, because they cannot overcome such constraints. SIDS must adopt strategies that reflect their usually limited administrative and political capacity and to strike a balance between the level of ambition, the available capacity and competence.

SRC is recommended as the generally the most appropriate form to provide BS to SIDS due to often a single dominant sector being present in the country[8] however as discussed later, GCCA budget support has also been provided to SIDS in the form of general budget support.

2.3 ELIGIBILITY REQUIREMENTS

Meeting eligibility requirements for EU BS has been recognised as a difficulty for SIDS, not due to having poorer economic governance, but due to having limited capacity to undertake the administrative work to establish eligibility, conducting dialogue and monitoring the program[9]. In recognition of this the guidelines have been narrowed down to make them more relevant to the situation in SIDS. There is a requirement to consider the four cross-cutting issues that have been identified above(in section 2.2) in assessing any application for BS by a SIDS. In addition any assessment of a SIDS application for budget support operation should take into account the size of the island population, the capacity in terms of development and the size and capability of the island administration. Below is a synapsis of the eligibility requirements specifically adjusted for SIDS.

<u>Stable macro-economic framework:</u> To meet this eligibility criteria recipient countries will need to be able to demonstrate that the government's fiscal policy and fiscal targets are consistent with macroeconomic stability. In particular fiscal policy needs to be transparent and any government debt sustainably managed. The current guidelines emphasise the requirement to mobilise domestic revenue, particularly where there is potential for revenue from natural resources. An assessment is made as to whether there is consistency between the three major elements of macroeconomic stability, fiscal policy and public financial management –particularly tax administration.

The assessment therefore should:-

- Analyse the main macroeconomic aggregates and identify potential sources of instability that would endanger the strength and the persistence of growth, or the return to a stable macroeconomic frame and debt sustainability;

- assess macroeconomic and fiscal policies in place and their contribution to stabilize the macroeconomic frame work over the short and medium term;

- assess efforts to strengthen domestic revenue mobilisation;

- assess vulnerability to external shocks and efforts to strengthen macroeconomic resilience.

For SIDS the assessment can be based on the most recent IMF Article IV reports or those prepared by the ADB or a regional authority. In small economies the assessment will take into

[8] Op.cit. Guidelines…, Annex 10
[9] *Ibid.*

account the institutional framework (such as the Central Bank) in terms of policy instruments and capacity.

<u>National/sector policies and reforms:</u> Potential recipients need to embrace a policy focus that clearly embraces sustainable growth and poverty reduction. In particular policies which have elements of[10]:-

- people's ability to participate in, and benefit from, wealth and job creation
- promote a 'green economy' that can generate growth, create jobs and help reduce poverty by valuing and investing in natural capital
- contribute to improving the resilience of developing countries to the consequences of climate change
- increases access to quality health and education services and strengthen local capacities to respond to global challenges

These policies need to be consistent with two cross-cutting issues. These issues are Tax collection, which needs to demonstrate a high degree of justice and fairness and expenditure allocation which has to have a focus on pro-poor, gender, and children issues. Importantly for this assessment the eligibility criteria implicitly identifies responses to the consequences of climate change, in the country's national policy statements, as a focus area.

It is recognised in the guidelines that whilst detailed sector policy may not be available in SIDS most have national development policies or strategies. A requirement is that the development policy addresses the four cross-cutting issues identified in section 2.2 and these be addressed to some extend in sector/development policy.

<u>Public financial management:</u> An assessment of the PFM environment in the recipient country will be undertaken by the EC prior to establishing any BS program. The assessment will examine the PFM institutions in the country, the legislative and regulatory framework governing PFM and past PFM in the country. From this assessment a baseline of PFM is established on which the implementation of reforms can be monitored. It is usually an approach which is adjusted according to the policy dialogue, capacity development in the country and the conditions of the financial transfers.

The Commission considers a country to fulfil the PFM eligibility criterion for programme approval when a credible and relevant programme to improve public financial management can be demonstrated to be in place. This usually requires assessment of:-

- A recent PEFA assessment or diagnostic study of the SIDS PFM
- Audited annual accounts
- A PFM reform program
    - Assessed for weakness, relevance and credibility
- Findings of the supreme audit institution
- Sector financial issues (if a SRC)
    - Procurement systems

[10] Communication from the Commission to the European Parliament, The Council, The European Economic and Social Committee and the Committee of the Regions :- *Increasing the impact of EU Development Policy: an Agenda for Change*, p.7 , Brussels, 13.10.2011 COM(2011) 637 final, European Commission

- Payroll performance
- Off-budget funds
- Level of fiscal decentralisation

This requirement is quite complex and examines the fiduciary risk associated with the quantum of funding being proposed. The risk is different depending on whether it is for general budget support or focused on a sector program, the proposed use that the transferred funds support (Technical assistance, Operational or capital expenditures etc.). The complexity of the assessment increases if more than a single donor is providing BS and there is a requirement to track individual donor related expenditures.

To accommodate improved PFM capacity in small SIDS the focus of the assessment will be on the analysis of shortcomings of existing systems and practices and then the establishment of priorities for reform, identification of resource constraints and development of coherent and well-paced implementation plans. In reasonably well performing SIDS the focus of the eligibility assessment will be more about assessing progress towards advanced reforms to achieve high PFM standards that can deliver, in addition to financial compliance and aggregate fiscal discipline, efficient and effective service delivery[11].

Transparency and oversight of the budget: This is the most recent inclusion into the eligibility criterion and follows from recognition of the role that the budget has in policy implementation. There is a requirement for countries to have a budget that is both transparent and available to the public for scrutiny. The Budget criteria are outlined in Table 1.

Table 1 Budgetary Information required for assessment[12]

Key Budget Document	Description	Release benchmarks	Comprehensiveness
Executive's budget proposal	The executive's budget proposal is the government's draft budget that should be submitted to the legislature.	Should be made available to the public when it is first presented to the legislature or, at a minimum, before the legislature approves it.	Should be presented within a medium term macroeconomic and fiscal framework, include all budgetary activities of the Government and detailed commentary on each revenue and expenditure programme
Enacted Budget	The enacted budget refers to the budget that has been passed by the legislature	Should be released to the public no later than three month after the legislature approves it	See executive's budget proposal.
In-year report	In-year reports (also Monthly Reports or Quarterly Reports) show progress in implementing the budget. These reports can be issued for the entire government or issued by different agencies.	Should be released to the public no later than three months after the reporting period	Should show the executive's progress in implementing the budge
Mid-year report	The mid-year report provides a more comprehensive update on the implementation of the budget.	Should be released no later than three month after the reporting period	Should include an update on the implementation of the budget, a review of economic assumptions, and an updated forecast of the budget outcome for the current fiscal year.
Year-end report	The year-end report is one of the key accountability documents. It shows compliance with the level of revenue and	Should be released no later than one year after the end of the fiscal year (the reporting period)	Should include the reconciliation with the approved budget and compliance with the revenue and expenditures

[11] *Op.cit.* Guidelines…, Annex 10
[12] *Ibid.* p. 41

	expenditures authorised by the legislature		authorised by the Parliament
Audit report	This report covers the year-end report audited by an independent Supreme Audit Institution.	Should be released no later than two years after the end of the fiscal year (the reporting period).	Should cover all activities under- taken by the executive following the adherence to appropriate auditing standards, and to the principle of interdependence of the external audit institution. Should focus on significant and systematic PFM issues and on performance such as reliability of financial statement s, regularity of transactions, functioning of internal control and procurement systems

Assessment of the most recently available budget information is undertaken, including the quality of the statistical system and budget data. From this an "entry point" is determined for this requirement. Countries have to show that they either provide the relevant information to the public or are making progress in a short period to do so. Particular allowances are made in relation to SIDS in meeting this criterion and for eligibility during implementation the guidelines state that more flexibility can be applied for SIDS, in particular with regard to the publication of the Executive's Proposal and the Year End Report or Audit Report. A program to gradually achieving full disclosure of budgetary information may be part of the reform program.

3 REQUIREMENTS FOR GCCA FUNDING THROUGH BUDGET SUPPORT

3.1 GCCA Budget Support eligibility requirements

Before a country can be considered for BS through the GCCA it must first meet the general requirements associated with GCCA assistance. These eligibility requirements for any form of GCCA assistance are prioritised as follows:-

- require a country to be one of the 73 LDS/SIDS countries that is a recipient of aid
- be vulnerable to climate change through floods, droughts, storms, sea level rise, glacier melting and the coastal zone elevation
- the proportion of the population at risk
- the importance of the agricultural sector (as assessed by the UN or other expert sources)
- an assessment of the adaptive capacity of the country (using the UNDP Human Development Index)
- an assessment on the country's engagement and dialogue on climate change issues
- the Government must express interest in receiving support from the GCCA

Funds are then allocated on the basis of availability and on population figures[13]

For GCCA consideration for assistance through budget support modalities it uses the common set of eligibility criteria as required for EU budget support[14] . An assessment will be required of the country's progress on macroeconomic stability, public financial management and implementation of the particular climate strategy being considered. For general budget support the national development plan/strategy will be used to assess climate change relevance. For sector budget support the reference will be the policies of the sector and how these relate to climate change. The assistance may have an objective of strengthening the integration of climate change into existing strategies or it may have the objective of developing a climate change strategy.

When the GCCA was first established the use of BS as an appropriate modality was highlighted and countries were selected for assistance in a pilot phase[15]. The proposed criteria included those outlined above in section 2.3. Most importantly they were countries that were already receiving or were in the process of receiving general/sectoral budget support through the EU or other donors. In the most recent review available all current BS programs are in countries where budget support and related conditions were or are already in place[16].

In conclusion the GCCA does not have a unique set of eligibility for assistance through a budget support modality. It uses the eligibility requirements developed by the EU and assesses a country application on a case by case basis. The most significant requirement for GCCA consideration of a request for budget support is the extent to which the proposed assistance aids in integrating climate change issues into the national/sectoral plans, strategies and budgets.

3.2 FUNDING EXAMPLES OUTSIDE THE REGION

Four countries are recipients of general budget support from the GCCA these are Mauritius, Seychelles, and Lesotho and within the Pacific the Solomon Islands. The assistance is to assist in overall development and poverty reduction and the common indicators being used are the setting up of processes, co-ordination structure or the passage of policy in the form of laws or regulation that are related to climate change. Mauritius and the Solomon Islands will be discussed separately in the next section.

The Seychelles is receiving €2.0 mil in general budget support and this is for mainstreaming climate change into policy and to assist in establishing an institutional and legal framework around mitigation measures in the energy sector. The project started in 2010 and completed in December 2012. Importantly prior to being provided the assistance under the GCCA programme the Seychelles had already qualified for general budget support under the *Vulnerability Flex allocation 2009*[17].

Lesotho is also earmarked for GCCA general budget support of €4.0 mil to run from 3013 to 2016. It is for mainstreaming climate change into development policy with and overall objective of development and poverty reduction. Similarly to the Seychelles, Lesotho has been involved in developing EU assistance through general budget support since 2006[18]. Progress in Public Financial Management Reform that has been underway since 2006 has assisted in the country has improved its ability to meet eligibility requirements.

[13] Using Innovative and Effective Approaches to Deliver Climate Change Support to Developing Countries, p.5, GCCA, EU 2011
[14] *Op.cit.* Paving the way…,p.42.
[15] *Op.cit.* Implementation framework, p.11
[16] *Op.cit.* Paving the way, p.48
[17] Commission Decision, PE/2009/9606 C(2009) 9917 of 11 Dec 2009
[18] See the Lesotho Country Strategy Program 2008-2013

Sector Budget Support programs have been supplied to a further four countries under the GCCA. These are Bhutan, Guyana, Rwanda and Samoa. The Samoan assistance will be discussed separately in the next section.

In Bhutan the budget support program is for €4.40 mil and is focused on mainstreaming climate change into development planning through the Renewable Natural Resources Sector. Most of the other donors supporting Bhutan, and in particular EU Member States such as Denmark, the Netherlands and Austria, are already providing budget support. The assessment of the EU eligibility criteria for sector budget support was conducted in January 2010. It was based to large extent on the 2009 IMF Article IV consultations as well as the PEFA-based PFM assessment carried out jointly by the Government and the World Bank throughout 2009[19].

Guyana has received €4.16 mil in GCCA sector budget and project based support directed at adaptation and REDD actions associated with climate change. The assistance started in December 2009 and is due to conclude in August 2014. Guyana has been a recipient of assistance in the form of non-targeted budget support since the 9th EDF (2002-2007) and this has been seen as an efficient aid delivery mechanism in the country[20].

Rwanda is the recipient of €4.55 mil in GCCA sector budget support for adaptation strategy to climate change in the land management sector. The timeframe for the assistance was from 2010 to 2012. It involved assistance for the Implementation of the Strategic Roadmap for Land Tenure Reform and the Strategic Plan for Environment and Natural Resources both of which were existing strategies. The EU has been providing budget support to Rwanda since 1999. Since 2009, general budget support has been framed in a Millennium Development Goals (MDG) Contract[21].

Therefore to conclude in all of the five countries reviewed above that were recipients of GCCA budget support all of them were pre-existing recipients of direct budget support, either through the EU or from bi-lateral partners. Since the EU guidelines state that a single risk assessment will cover all budget support contracts in the same country[22], the presence of pre-existing budget support program that is monitored and the risk assessment updated will aid in facilitating budget support under GCCA financing.

4 PRECONDITIONS FOR GCCA PROJECTS FUNDED IN SMALL ISLAND DEVELOPING STATES (SIDS)

4.1 GENERAL BS PROGRAM MAURITIUS

Mauritius qualifies for budget support since it fulfils the eligibility criteria[23] and 98% of EU assistance to Mauritius is mainly delivered through General Budget Support. It has a well-defined macro-economic framework; transparent, accountable and effective public expenditure management and an open and transparent public procurement system.

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[19] Bhutan, Country Strategy Paper 2008-2013: Mid Term Review Document, !P 2011-2013, April 2010, EEAS

[20] Guyana, Country Strategy Paper and National Indicative Program (2008-2013), EC Delegation to Guyana, Suriname, Trinidad and Tobago and the Netherlands Antilles

[21] Source: *http://eeas.europa.eu/delegations/rwanda/eu_rwanda/devlopment_cooperation/budget_support_economy/index_en.htm*

[22] Budget Support Guideline, Executive Guide, p.8, Sept 2012

[23] As set out in the Cotonou Agreement Article 61.2

The EU has a long history of providing assistance to Mauritius through budget support programs, dating back to 2004. The Government has had a 10 year reform program that has been supported by the EU since 2007. The reform program targets higher economic growth by creating a new socio-economic model, driven by competitiveness and creation of opportunities for all.

Five budget support programs have been financed by the EU since 2004 one of which is the GCCA budget support program:

Sector Budget Support:

- Wastewater Sector Policy Support Programme (2004-2008) of € 38 million
- Sugar Sector Support Programme (2006) of € 11 million

General Budget Support:

- Improved Competitiveness for Equitable Development I and II (2007-2009) of € 119.25 million
- Promoting Sustainable and Equitable Development (2010-2012) of € 169.153 million
- Global Climate Change for Mauritius (2010-2012) of € 3 million

The objective of the general budget support programme 'Promoting Sustainable and Equitable Development (PSED)' is to contribute to the sustainable economic development of Mauritius. This is by maintaining, since June 2006, the support to the ten-year economic reform programme being implemented by the Government of Mauritius, which includes the re-structuring of the sugar sector. The specific objective of PSED is to encourage higher level results from the economic reform programme while mitigating the negative impacts on the environment and protecting the vulnerable groups through access to education and training.

The Global Climate Change general budget support programme (GCCA) of € 3 million was aimed at supporting initiatives in the sustainable development sector. The program complemented an existing loan programme of the Agence Française de Développement called Environment Aid Programme, which was a loan of € 125 million in support of the Maurice Ile Durable (MID) initiative. Under the GCC technical assistance has been provided for environment friendly buildings in Mauritius.

While the ICED I, II and the Global Climate Change Programmes for Mauritius have been completed, the Promoting Sustainable and Equitable Development is still on going.

The Budget support programmes have been regularly assessed and it is important in the context of budget support that the following have been achieved:-

- Satisfactory progress in the implementation of the economic reform programme, including high level structured policy dialogue on a regular basis covering key sectors and with key stakeholders;

- Satisfactory progress in maintaining a policy of macro-economic stability, as evidenced by EC's positive assessment of the macro-economic situation based on IMF article IV consultations;

- Satisfactory progress on implementation of the programme to improve and reform public finance management as indicated, inter alia, by progress in the implementation of measures taken by the Government to address weaknesses identified by the PEFA assessments;

Specifically in relation to the policy objectives of the GCCA assistance:-

- Adoption of the National Energy Strategy by the Government of Mauritius (Cabinet);

- Energy Efficiency Bill has been approved by Cabinet for introduction to Parliament; A draft Action Plan for the National Energy Strategy has been elaborated
- New Building Control bill that includes requirements for sustainable building is approved by Cabinet for introduction to Parliament;

The EU Delegation closely coordinates budget support operations and technical assistance with other development partners, namely the World Bank, the Agence française de Developpement , the African Development Bank and the UNDP.

4.2 SAMOAN WATER SECTOR SUPPORT

Samoa is receiving €3.0 mil in GCCA funding in the form of a sector budget support program over the period 2012-2015. It follows from a long EU association with the water and sanitation sector in Samoa that dates back to the 1995. The GCCA assistance is not the first agreement with the EU for direct budget support. The first budget support agreement was approved in December 2009 and was for €15.3 mil under the Annual Action Plan covering the period 2010 -2013[24].

The process of initially qualifying for budget support commenced with the Government of Samoa (GoS) requesting the EU to commission a preliminary assessment of the Samoan Public Financial Management (PFM) system based on the Public Expenditure and Financial Accountability (PEFA) PFM Performance[25].

In 2008 Samoa's Ministry of Finance launched the Public Financial Management Reform Plan (2008-2011). The PFM Reform Plan built on previous capacity building initiatives including the AusAID-financed Samoa Treasury Institutional Strengthening Project completed in 2001. The reform plan was based on the findings of the earlier PEFA Assessment and partly on GoS's own assessment of the public finance management system[26]. Therefore in terms of budget support Samoa had a baseline established for PFM in 2006 and a reform program in place to address PFM issues. Further in November 2009 GoS, Australia, ADB, the World Bank and NZAP agreed to the use of a joint donor Policy Action Matrix for disbursing general budget support.

The GCCA sector policy support programme in Samoa aims to strengthen the integration of climate change adaptation into the update of the Water for Life Sector Plan 2012-2016. The Water for Life strategy has been part of Samoa's national development strategy, the *Strategy for the Development of Samoa* for many years.

To summarise the situation in Samoa, it has qualified for budget support under the GCCA assistance because of the long association that the EU has with working in the Water and Sanitation Sector. This association includes the technical work associated with meeting the fiduciary requirements of budget support. Samoa was already the recipient of sector based budget support in the same sector prior to the GCCA assistance. The GCCA assistance allowed the integration of climate change issues into an already existing and successful program.

4.3 SOLOMON IS CLIMATE ASSISTANCE PROGRAM

The Solomon Islands is also a recipient of GCCA assistance. It has received €2.8 mil through general budget support. The assistance is to run from March 2011 to March 2014. It has been

[24] EU approves first Sector Budget Support Programme for Samoa, Europe Aid, 21 December 2009

[25] Samoa Public Finance management: Performance report, October 2006, Linpico

[26] Draft Discussion Note: Samoa Public Financial Management Reform Program (Performance Linked Aid), 2012, AusAID

provided to support effective mainstreaming of climate change and disaster risk reduction priorities in national development policies and in key sector strategies. It proposes the strengthening of the institutional capacity of the Ministry of Environment and National Disaster Management Office. A further objective is to ensure that budget allocations are made to the agencies responsible for climate change and disaster risk mitigation activities[27].

This general budget support to the Solomon's under the GCCA also follows from an earlier approval to provide budget support under another program. It contrasts to the situation in Mauritius and Samoa which in both earlier cases the EU had a long program of association in using direct budget support as the modality of assistance (Mauritius), or experience in progressively working the same sector (Samoa). In the Solomon situation neither of these preconditions appears to exist.

The stated focus of EU support in the Solomon's has been in capacity development in rural development under the Agriculture and Rural Development Strategy (ARDS), not environment or disaster management. Similarly in 2007 the PFM and budget systems in the Solomon's were assessed as having major weaknesses[28]. It concluded that there was no possibility of providing budget support because of the Solomon's inability to meet eligibility criteria due to weaknesses in in PFM and no credible reform program in place, there were also concerns about the Government's ability to maintain a stable macroeconomic environment.

The Solomon Islands however made a request to the EU for direct budget support under the Vulnerability Flex (V-flex) ad hoc mechanism[29]. It made this request in 2009 to compensate it for a severe drop in revenues. This form of budget support is a *State Building Contract (SBC)* and due to the immediacy of the required assistance a more forward looking approach in respect to policy and reforms is taken. It is also the same form of direct budget support that predated GCCA budget support in the Seychelles (Section 3.2)

The funding was approved in 2010 and the agreement contained the following "*The decision to provide assistance in the form of budget support stems from the appreciation by the donor community of SIG's recent reform efforts, in particular in public finance management, it's prudent macroeconomic policies, including in the face of a severe economic downturn, and its overall commitment to poverty reduction and economic growth. In parallel, and in line with the Methodology on Budget Support in Fragile Situations, a political and risk analysis has concluded that budget support was an appropriate aid modality to help Solomon Islands addressing its "fragile situation" and rebuild the state, and that risks were limited that a less-reform minded Government would emerge after the upcoming elections. Against this background, a road map to establish budget support eligibility was prepared, which has been on track up to now"*[30]

The approval was for €15.2 mil in direct budget support to be paid in the third quarter of 2010. In the assessment of qualifying for budget support in the period 2008-2009 the SIG had been seen as making good progress on PFM and policy setting, and partly as a consequence of the GEC, the reform path started by the authorities had therefore been perceived as having new impetus. The SIG strengthened its engagement with the donor community. These developments were regarded as being conducive to the start over the 2009 year general and sector budget support operations by the key development partners in

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[27] *Op.cit.* Using Innovative and effective approaches….p.28

[28] Solomon Islands: Country Strategy Program and National Indicative Program 2008-2013, p.22

[29] In reaction to the global economic crisis supporting developing countries in coping with the crisis (COM 2009-160) foresees inter alia the creation of the V-Flex mechanism to support the most vulnerable and least resilient ACP countries in coping with the impact of the global financial crisis.

[30] Solomon Islands - Solomon Islands Economic Recovery Assistance (SIERA) Programme CRIS Number FED/2010/022-271,p.1, 2010

the country (Asian Development Bank, Australia and New Zealand, with the World Bank thought likely to follow). Therefore the decision was made in mid-2009 by the EU to channel the resources from the V-Flex through budget support.

Taking into account the Methodology for Budget Support in Fragile Situations, the EU considered that there were good prospects of donor coordination and policy dialogue under a budget support program. Based on this assessment Solomon Islands were regarded as meeting the eligibility conditions to budget support and was expected to maintain these conditions during the formulation and the implementation of the program.

As discussed earlier the 2008 PEFA report for the Solomon Islands indicated major weaknesses in the PFM and budget systems[31]. Responding to this review the SIG established in March 2009 the Solomon Islands Core Economic Working Group to better co-ordinate the economic and financial reforms. It is assumed that the progress made on these reforms[32] that was co-ordinated with donors aided in reversing the earlier assessment that the Solomon Islands was not a suitable candidate for direct budget support.

In summary the GCCA direct budget support to the Solomon's is consistent with the findings of all the other GCCA examples of providing direct budget support, an existing direct budget support program was already in place. The Solomon's situation differs from the other two SIDS examined in that it did not initially qualify for budget support under EU guideline requirements. These requirements however seem to have been relaxed due to the nature of the direct budget support modality (SBC) sought by the SIG under the V-flex arrangement. It is this relaxation of the strict (particularly PFM and Budget) requirements of the guidelines in this initial funding that appears to have facilitated the later assessment requirements under the GCCA.

[31] Solomon Islands: Public Financial Management, Management Report, ECORYS, Nov 2008

[32] Report of the Economic & Financial reform program, SICEWG, 2nd Annual Joint Review, Oct 2011

Annex 1

Review and assessment of national and sector policies in relation to budget support modalities in the Pacific Smaller Island States:
Sub-component to review and assess preconditions for projects funded through the Global Climate Change Alliance in the Pacific and SIDS regions using budget support modalities.

a) Background to the specific work covered under this consultancy

The European Union (EU) established the Global Climate Change Alliance (GCCA) in 2007 to strengthen dialogue, exchange of experiences and cooperation on climate change with developing countries most vulnerable to climate change, in particular the Least Developed Countries and the Small Island Developing States (SIDS). GCCA is the main implementing channel for the EU fast start commitments related to climate change adaptation. Under funding allocated in 2010, €11.4 million has been allocated to the GCCA: PSIS Project.

The **overall objective** of the SPC GCCA: PSIS is to support the governments of nine smaller Pacific Island states, namely Cook Islands, Federated States of Micronesia, Kiribati, Marshall Islands, Nauru, Niue, Palau, Tonga and Tuvalu, in their efforts to tackle the adverse effects of climate change. The **purpose of the project** is to promote long-term strategies and approaches to adaptation planning and pave the way for more effective and coordinated aid delivery to address climate change at the national and regional level.

The GCCA: PSIS project is implemented by SPC as part of its 'whole of organization approach' and is one of the activities contributing the SPC Climate Change Engagement Strategy. The four key result areas (KRA) are:

- KRA 1: Supporting national efforts to successfully mainstream climate change into national and sector response strategies.
- KRA 2: Identifying, designing and supporting the implementation of adaptation activities.
- KRA 3: Enhancing the contribution of regional organisations to national adaptation responses.
- KRA 4: Building regional capacity to coordinate the delivery of streamlined adaptation finance and targeted technical assistance to countries

The project will assist the nine countries design and implement practical on-the-ground climate change adaptation projects in conjunction with mainstreaming climate change into line ministries and national development plans; thereby helping countries move from an *ad hoc* project-by-project approach towards a programmatic approach underpinning an entire sector. This has the added advantage of helping countries better position themselves to access and benefit from new sources and modalities of climate change funding, e.g. national and sector budget support.

A team of consultants have been recruited to conduct an assessment of the extent to which climate change is mainstreamed in national and sector policies in Cook Islands, Federated States of Micronesia, Kiribati, Marshall Islands, Nauru, Niue, Palau, Tonga and Tuvalu so as to inform the delivery of funds via modalities such as budget support in the context of the Global Climate Change Alliance notably. This work is scheduled to take place between June and August 2013.

This present consultancy will complement the work of the team already contracted by focusing on requirements for EU budget support, and reviewing preconditions that had to be in place for other

GCCA projects in the Pacific and other SIDS regions (Indian Ocean and Pacific) that have been funded through budget support modalities.

The information gained from this assessment will be shared with country and other representatives from the climate change and financial management communities at a regional meeting 25-27 September 2013. (This sharing event is not a part of this present expression of interest).

Linkages will be made between this consultancy and ongoing work in the area of climate change finance in the Pacific being undertaken by regional and international organisations.

b) Scope

The purpose of this consultancy is to: (a) review requirements for climate change finance through budget support especially as required by the European Union (EU); (b) review pre-conditions required for at least three other GCCA projects in the Pacific and other SIDS that have been funded through budget support modalities; (c) provide input to the national review reports being prepared by the firm already contracted.

c) Specific activities

The consultant(s) will undertake a desktop study to include the following:

1. Consult with the firm already contracted and prepare a schedule and work plan for the activities to be undertaken. (The Director of the firm already contracted is the Lead in the overall consultancy: Review and assessment of national and sector policies in relation to budget support modalities in the Pacific Smaller Island States).
2. Prepare a concise report describing (a) the eligibility requirements for EU budget support and (b) the eligibility requirements for GCCA funding through budget support.
3. Review the preconditions required in at least three countries that have qualified for GCCA budget support in the Pacific, Indian Ocean and Caribbean regions (suggested countries are Mauritius, Samoa and Solomon Islands).
4. Using the foregoing analysis in (2) and (3) provide comments and relevant input to the national reports being prepared by the firm already contracted on the extent to which climate change is mainstreamed in the national and the selected sector policies of the nine project countries, and help identify further work that needs to be undertaken by the countries in the 2013-2015 time frame.

d) Outputs

The outputs of this consultancy are as follows:

1. A well-articulated schedule and work plan.

2. A concise report describing (a) the eligibility requirements for EU budget support and GCCA funding through budget support.

3. A concise report on preconditions required in three countries that have qualified for GCCA budget support in the Pacific and Indian Oceans.

4. Documented input to the national reports on climate change mainstreaming being prepared by the firm already contracted.