DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSAL FOR SECTOR-WIDE APPROACHES (SWAPS)

AUGUST 26, 2004

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EXECUTIVE SUMMARY

1. This document presents a proposal for Sector Wide Approaches (SWAps). A SWAp is an approach by which all development partners[1], involved in a sector, collaborate to support a single government-led sector policy and expenditure program, adopting common approaches across the sector, and progressing towards relying on government procedures to disburse and account for all funds. A SWAp is not a lending instrument but rather an approach that can be supported by any of the Bank's investment lending instruments.

2. The funding arrangements used by SWAps are either pooled funding (or basket funding), non-pooled funding, and/or a combination of these. Under pooled funding the government and/or development partners deposit their funds into and disburse from a common account rather than using their own special-purpose accounts. Pooling of funds requires that all participants use common procurement, financial management and disbursement procedures. Funds that are not pooled are placed in special purpose accounts for each financier, as is customary for traditional investment loans, and follow the disbursement, procurement and financial management rules and procedures of each participating financier.

3. Although the Bank can presently participate in SWAps, it cannot currently use two of its increasingly attractive features. First, it may not partake in pooled funding, since Bank policy requires that its loan proceeds be placed in a special, separate account and that the Borrower track the sources and uses of all Bank project funds. .Second, the Bank's financial management, disbursement, and procurement procedures need to be followed in all Bank operations. This document proposes that, when the Bank participates in a SWAp, it be granted the option of pooling its funds in a common account with the government and/or with other participating development partners, and that the transactions it finances through the pooled account be those falling below the Bank's threshold for international competitive bidding (ICB) for goods, works, and consulting services. In addition, the document proposes that consideration be given to also harmonizing procurement, financial management and disbursement procedures with other financiers when funds are not pooled, and, to the extent possible, use country systems when these are satisfactory. At this stage, this would be done on a project-by-project basis, and only in those cases where the alternative procedures provide equal assurance regarding adequate use of loan proceeds, and would likely increase the development impact of the operation.

4. Bank participation in pooled funding would require the following exceptions to Bank policies and procedures: no special account would be created for Bank loan proceeds; supporting documentation for individual transactions financed by the pool would not be regularly submitted to the Bank; financing of eligible expenditures in the pooled account would not be restricted to goods, works and consulting services that comply with the Bank's requirement that the nationality of bidders and origin of goods be from member countries; and goods, works and consulting services financed from the pool would follow national procurement rules and procedures, or other rules and procedures jointly agreed by all participants, provided they are governed by principles of economy, competition, transparency, publicity, equality and due process.

[1] In this context, development agencies or development partners refers to multilateral development banks, international organizations, government aid agencies, NGOs or any other entity that participates in the financing of a SWAp either through grants or loans.

A. Background

1.1 At its meeting of June 3rd 2004, when discussing *An Approach for Further Development of Lending Instruments and Operational Policies* (GN-2272-1), the Policy and Evaluation Committee of the Board of Executive Directors agreed that Management prepare a proposal for Sector Wide Approaches (SWAps). This document presents this proposal.

1.2 An inter-departmental working group consisting of representatives from the three Regional Operations Departments, LEG, SDS, ROS and DPP took part in the elaboration of this proposal. Different sources were used as inputs in its preparation. An extensive review of the literature on SWAps was conducted and staffs from other Multilaterals Development Banks and bilateral development agencies with experience in SWAps were consulted. In addition, SWAps were discussed with Borrowers and country office staff to get their opinions on aspects to consider while developing this SWAp proposal.

B. Rationale

1.3 A sector wide approach (SWAp) is an approach by which development partners collaborate to support a government-led program for a sector or sub-sector in a comprehensive and coordinated manner. Under a SWAp "all significant funding for a sector supports a single sector policy and expenditure program, under government leadership, adopting common approaches across the sector, and progressing towards relying on government procedures to disburse and account for all funds."[2] This approach evolved from the traditional investment project as a means to increase the development impact of donor resources, decrease the transaction costs of recipient countries, and strengthen the Borrower's institutions in managing all the sector's resources. A SWAp is thus not a new lending instrument but rather an approach that can be supported by any of the Bank's investment lending instruments.

1.4 Most MDBs now feature SWAps among their lending modalities. The bilateral donor community has also been using the approach to finance its development programs, and has requested IDB involvement through the harmonization work program. In addition, SWAps are increasingly being seen by the international donor community as an effective tool to harmonize development financing, encourage the use of country systems and strengthen them where needed. Significant efforts are now underway in the harmonization exercise among MDBs and donors to harmonize SWAps, and there is preliminary agreement to prepare joint MDB SWAp guidelines.

1.5 Demand for SWAps has been steadily increasing in recent years, both from lower and middle-income countries. At the World Bank, for example, five substantial SWAp loans were approved in 2004 alone, two of which were for Latin America. In addition, numerous others are under preparation. The IDB has also been approached by various Borrowers to participate in SWAps.

1.6 The growing Borrower demand for SWAps has been a result of the advantages they provide and the features they offer. First, by supporting the government's development vision for the sector, they strengthen country ownership and leadership. They provide development cooperation within a single agreed-upon sector strategy and expenditure program, reducing

[2] "New Approaches to Development Co-operation: What Can We Learn from Experience with Implementing Sector Wide Approaches?", Mick Foster, Overseas Development Institute, London, UK. October 2000.

duplication of efforts and increasing resource allocation efficiency and development effectiveness. SWAps also improve donor coordination and harmonization of procedures, significantly reducing Borrower transaction costs. In addition, they enable Borrowers to institute a single procurement, financial management, and disbursement system, thereby reducing the administrative burden of parallel systems. Finally, by emphasizing the use of government procedures, SWAps provide a real opportunity to strengthen the country's own capacity, systems and institutions. In sum, adding SWAps to the Bank's lending modalities would respond to Borrower demands, keep the Bank competitive with other development partners in the Region, align it with the emerging trends among MDBs and the international donor community, and help strengthen country systems and institutions.

C. Description and Characteristics

1.7 Since their emergence in the 1990s SWAps have been continuously evolving. Different SWAps have included varying features depending on the sector context, the composition of the participating development partners, the fiduciary risk involved and the local capacity. Overall, however, SWAps share the following characteristics:

1.8 *Country Leadership and Ownership*: In a SWAp, development partners join to support the government's own development program for a particular sector. The government directs the program and mobilizes and coordinates the different sources of financial and technical support for sector development.

1.9 *Collaborative Process*: SWAps require partnership and close coordination between the government, development partners and other relevant stakeholders, as well as a commitment on the part of all parties to openness, consultation, and sharing of information.

1.10 *Agreed Sector Policy Framework*: Fundamental to a SWAp is the existence of a single comprehensive sector policy framework that is agreed among the government, all development partners involved in the sector, and other key stakeholders. The policy framework defines the overall goals, principles and priorities for the sector, which are translated into a medium-term (typically five-year) sector strategy outlining the sector's objectives and means to achieve them. The medium-term strategy is articulated into a program of specific interventions over a given period of time. Annual activity programs are jointly reviewed each year and adjusted as deemed necessary. All development partners and the government agree on the proportion of the program that each will finance. In principle, by agreeing to support a common sector program, development partners agree *not* to finance expenditures outside the agreed program, so that resources are concentrated on the agreed priorities. Likewise, the government is expected not to accept donor financing for the sector which falls outside the framework agreed.

1.11 *Expenditure Framework and the Resource Envelope:* The sector policy framework and the government's overall medium-term public expenditures are used to define an expenditure framework and resource availability for the sector. The expenditure framework is a key mechanism for ensuring that an adequate level of resources is available to the sector and is allocated to finance expenditures in priority areas to achieve greater impact at the sector level. The sector policy framework, the activity program and the expenditure program can be refined or adjusted over time in response to lessons learned and other relevant information, or to address specific issues that might arise during the implementation of the SWAp.

1.12 *Harmonized Appraisal and Implementation Mechanisms and Use of Local Systems and Procedures*: Harmonization and alignment are major underlying principles essential to the design of a SWAp. Development partners aim to harmonize their own preparation and implementation processes through joint programming, appraisal, reviews, monitoring and evaluation, and attempt at having a single procurement, financial management, disbursement, reporting and auditing system. Rather than creating parallel systems, the emphasis is on using and strengthening the government's own institutions, procedures, systems and staff.

D. Funding Arrangements

1.13 SWAps use various funding arrangements that can be classified into pooled funding (or basket funding), non-pooled funding, and/or a combination of these. Whether or not pooled funding is used in a SWAp, or the extent to which it may be used in a particular operation, is typically a function of factors such as the composition of development partners, fiduciary risks, local capacity, and transaction costs involved.

1.14 *Pooled Funding*: Pooled funding refers to an arrangement whereby the government and/or development partners participating in the SWAp deposit their funds into and disburse from a common account rather than using their own special-purpose accounts. Pooling of funds requires that all participants use common procurement, financial management and disbursement procedures. Harmonization of procedures in pooled funding is carried out in two ways. The first and preferable way is for the government, itself, to manage the pooled account, using its own procurement and financial management procedures. The second way is to use common financier procedures agreed by all parties, and for one financier to manage the account on behalf of the others. This arrangement is usually adopted in cases when the fiduciary risk of using country procedures is very high and the measures to mitigate this risk could significantly delay implementing the operation.

1.15 *Non-Pooled Funding*: Funds that are not pooled are placed in special purpose accounts for each financier, as is customary for traditional investment loans. In addition, they usually follow the disbursement, procurement and financial management rules and procedures of each participating financier. There could be instances, however, where harmonization of some of these procedures may already take place among development partners and/or the government. In those cases common procedures could be used for non-pooled funding. It is expected that as the harmonization process among MDBs and other financiers continues to progress, common procedures for procurement, disbursement and financial management for out-of-pool funding is likely to increase.

E. Fiduciary Arrangements

1.16 The fiduciary arrangements used in SWAps need to provide sufficient assurances that program resources are used effectively and for their intended purposes. In addition, they are intended to reduce the transaction costs to Borrowers by minimizing the use of separate financier requirements, and contribute to strengthening Borrower procurement and financial management capacity. This becomes particularly important when pooling of funds is used.

1.17 The fiduciary arrangements of a SWAp require the following: fiduciary risk assessments and mitigation measures, financing arrangements, monitoring and auditing, and agreement among financiers on all these items. During the preparation phase of a SWAp, joint government-financier procurement and financial management assessments of the sector institutions involved should be undertaken. These assessments should ascertain the country's financial management and procurement capacity, identify any weaknesses, and propose measures to strengthen these systems and mitigate any risks to financiers. In addition, the assessments should take into account the findings of any country-level fiduciary assessments or diagnostic studies that might already exist (Country Procurement Assessment Reviews, Country Financial Accountability Assessments, Public Expenditure Reviews, among others).

1.18 The findings of these assessments should be shared among all parties who must reach an agreement on the procurement, financial management, and disbursement systems to be used by the program. Participating financiers also need to reach agreement on the funding arrangements (i.e. pooled funding or non-pooled funding) and on how each financier will contribute to the SWap (i.e. timing, share, mechanism, etc.). Finally, if there are plans to strengthen the Borrower's financial management and procurement capacity and/or mitigate risks to financiers, the parties will need to agree on these plans and on how their implementation will be monitored during execution.

1.19 Throughout project implementation, the Borrower and participating financiers should jointly monitor the procurement and financial management of the SWAp through regular reviews of reports and audits agreed by all parties.

F. Proposed Bank Participation in SWAps

1.20 There are no impediments in terms of policy, rules and procedures to Bank participation in SWAps. In fact, it has already been involved in numerous operations that have followed a SWAp-like approach. For example, the Bank has participated, through cofinancing, in operations whereby all development partners followed a single agreed sector strategy and expenditure program, and harmonized project preparation and implementation requirements and procedures. Time-slice operations have also contained SWAp features, by financing segments of the government-led medium-term investment plan for the sector or subsector, and periodically reviewing and adjusting the investment plan as needed.

1.21 Although the Bank can presently participate in SWAps, there are two increasingly attractive features of SWAps that it may not currently use. The first of these features is pooled funding. The Bank cannot currently partake in pooled funding, since Bank policy requires that its loan proceeds be placed in a special, separate account and that the Borrower track the sources and uses of all Bank project funds. The second feature involves using the fiduciary procedures of the country or harmonizing with those of other participating financiers. Bank norms require that all its investment loans follow Bank financial management, disbursement, and procurement procedures.[3]

1.22 With respect to pooling of funds, it is proposed that when the Bank participates in a SWAp, it be granted the option of pooling its funds in a common account with the government and/or with other participating development partners, so as to be able to participate fully and equally with other financiers, and under the same, comparable conditions. The next section more fully explains the reasons behind this proposal and elaborates on how Bank participation in pooled funding should be undertaken.

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[3] The exception is the Performance-Driven Loan, which allows national procurement procedures to be followed as long as these are governed by principles of economy, competition, transparency, equity, publicity and due process. (GN-2278-2)

1.23 Consideration could also be given to harmonizing procurement, financial management and disbursement procedures, with other financiers when funds are not pooled, and, to the extent possible, use country systems when these are satisfactory. However, at this stage, this would be done on a project-by-project basis, and only in those cases where the alternative procedures would provide equal assurance regarding adequate use of loan proceeds, and would likely increase the development impact of the operation.

1. Proposal for Participation in Pooled Funding

1.24 Participation in pooling is considered important because of the advantages that it offers to both the Bank and the Borrower. The use of a single procurement, financial management and disbursement system instead of parallel systems, significantly reduces transaction costs and the "hassle factor" for Borrowers. In addition, it strengthens the government's own procurement and financial management systems, thereby enhancing country ownership, and better contributing to the development of sustainable country fiduciary capacity. Pooling also ensures more timely availability of resources for program execution, provides greater resource predictability, and streamlines the flow of project funds.

1.25 For the Bank, pooling would offer the opportunity to strengthen its relationship with the Borrower in a particular sector over the long-term. It would enhance the Bank's development impact by shifting Bank supervision from tracking funds through loan proceeds to oversight and improvement of the Borrower's fiduciary systems. In addition, pooled funding encourages the harmonization of financial management, procurement and disbursement systems among development partners. In this regard, there has been increasing pressure from the international community, particularly from bilateral development agencies, for the Bank to participate in pooling of funds. Other MDBs such as the World Bank and Asian Development Bank are actively participating in pooled accounts through their SWAps. Furthermore, Borrower demand for SWAps with pooled accounts has been rapidly increasing, particularly on the part of the middle-income countries. At the World Bank, for example, three SWAp operations with pooled funding have been approved for middle-income countries in 2004, two of which are in Latin America. In addition, numerous others are in preparation. Bank participation in pooled funding would address Borrower demand and help the Bank to remain competitive with other financiers who are presently supporting our Borrowers.

a) Transactions Financed by a Pooled Account

1.26 The transactions that could be financed through pooled funding would include those falling below the Bank's threshold for international competitive bidding (ICB) for goods, works, and consulting services. All transactions financed through the pool would follow common procurement, financial management and disbursement rules and procedures agreed upon by the government, the Bank and all other partners participating in the pooled account.[4]

1.27 To the extent possible, the Borrower's procurement and financial management rules and procedures would be used. More specifically, the Bank could participate in a pooled account

[4] It is worth noting that as a result of the harmonization process among MDBs and other financiers, differences between the procurement rules and procedures of financiers for ICB transactions are progressively diminishing. This could eventually allow for also using a common set of procurement rules and procedures for ICB transactions in a SWAp.

that applies national procurement rules and procedures, provided the sector institutions responsible for the execution of the SWAp follows procurement practices and procedures that are governed by principles of economy, competition, transparency, equity, publicity and due process. Likewise, the Bank would need to ensure that the financial management system (including accounting, reporting, auditing and internal controls) of the sector institutions implementing the SWAp provide accurate, timely and reliable information regarding the SWAp's resources and expenditures. If fiduciary weaknesses exist in the sector, it may be necessary to set up transitional financial management and/or procurement arrangements for the project's proceeds until such time as sectoral systems are strengthened and the fiduciary risk mitigated. Transitional arrangements could include, for example, greater supervision by development partners, increasing the frequency and adjusting the scope of audits reports, or providing technical assistance. It is important that these transitional arrangements be subject to an agreed timeline for moving towards using the Borrower's fiduciary systems.

1.28 At appraisal the government, the Bank and all other development partners participating in the SWAp would agree on the overall operational program for the operation, and identify those activities to be financed from the pooled account. Agreement would also be reached on the proportion that each financier participating in the pooling would contribute to the pooled account over the life of the project. The Bank's proportion would be established based on an ex ante estimation of the proportion of pooled expenditures that would be eligible for Bank financing. The established share of Bank financing would be set below the proportion of total eligible expenditures estimated for financing from the pool. Each year when the annual operational plan for the SWAp is reviewed, the government would provide to the Bank and all other participating development partners, for their review and concurrence, a procurement plan that would include the specific procurements to be carried out for the following year, the method of procurement and source of funding (pooled account or non-pooled financier funding).

b) Disbursements

1.29 The Bank would disburse funds into the pooled account in the proportion agreed upon between the government and all participating financiers. Disbursements could be provided either as advances or reimbursements, and would be released based on consolidated Financial Monitoring Reports (FMR) whose preparation would be under the responsibility of the Borrower. These reports would be provided quarterly (or whatever frequency is agreed-upon) to the Bank and other participants in the pool and would cover the entire program. They would present the program of activities and resulting expenditures incurred in the previous period and an activity and expenditure plan for the following period. Supporting documentation for the individual transactions financed from the pool would not be submitted to the Bank or other financiers. In addition, the pooling of all participating financiers would not allow the tracking of expenditures attributable to any one financier. The Borrower, however, would be required to maintain adequate records of the transactions financed from the pool, and the Bank would reserve the right to request and review this documentation when and if deemed necessary.

1.30 The degree of expenditure detail included in the FMR would be agreed among the Bank, the government and other participants. The FMRs would be subject to external audits which would be done annually or more frequently, if so agreed by the Bank and other participating partners.

1.31 Throughout the execution of a SWAp the Bank would need to ensure that the proportion of its contribution to the pooled account was less than the total of eligible expenditures actually incurred. The FMRs (and any equivalent reports prepared in agreement with the government and other partners) and FMR audits would be the sources used in this verification. If it is determined that the Bank funds disbursed into the pooled account exceeded the eligible expenditures financed through the pool, or that some of the incurred expenditures were not eligible, the Bank could request the Borrower for a refund of the amount(s) disbursed, reduce its future replenishments to the pooled account, or exercise any other measure it deems necessary.

1.32 During project appraisal the Borrower, the Bank and all other partners participating in the SWAp would need to come to an agreement on the frequency and content of the consolidated financial monitoring reports. In addition, agreement would need to be reached regarding auditing arrangements including frequency, format and content of audit reports, eligibility criteria for auditor selection, and follow-up of audit recommendations.

c) Procurement

1.33 Procurements financed by pooled funds would be subject to an "ex-post" review. The government, Bank and all partners participating in the pool would agree on an ex-post supervision plan specifying the frequency of the reviews, the procedure to be used, and those responsible for undertaking the reviews. The Bank and all other partners would receive copies of the reviews.

1.34 If the ex-post reviews reveal that the procurement process of any contract financed by the pooled account, failed to adhere to the procurement procedures agreed by the parties, the Bank would reserve the right to cancel from its loan or request reimbursement of the amount equal to the contract amount times the Bank's percentage participation in the pooled account. The other participating development partners would need to make the same determination with respect to their respective financing of the contract.

1.35 It is proposed that Bank financing of eligible expenditures covered by the pool not be restricted to expenses resulting from the procurement of goods, works and consulting services by member countries of the Bank. There are several reasons for this proposal. First, the proportion that each financier participating in the pool contributes to the pool would be defined prior to project approval and is based on a projected program of activities for the SWAp. Since, at that particular moment in time, the procurement process for the operation would not yet have taken place, it would not be possible to determine which expenditures would be procured by suppliers of Bank member countries and which would not. Second, the Borrower would have to provide to the Bank the necessary information in order for the Bank to confirm that the origin of goods, works and consulting services financed by the Bank from the pooled account had derived from member countries. This would increase the transaction costs to the Borrower and act in a way contrary to harmonizing and using country systems, going against the spirit of a pooled account. Finally, it would move the Bank towards greater harmonization with the World Bank, which finances expenditures resulting from the procurement of goods, works and services by all countries. [5]

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[5] *Guidelines. Procurement under IBRD Loans and IDA Credits*, World Bank, May 2004.

2. Environmental and Social Safeguards

1.36 The SWAp would be subject to social and environmental standards that are consistent with the environmental and social safeguards of its financiers. In keeping with the spirit of a SWAp, the Bank and other development partners would rely on Borrower systems to the extent possible. During the preparation phase, a strategic environmental assessment at the sector and program level would be undertaken. The assessment would identify the appropriate enabling conditions for environmental sustainability, and would examine the policy framework and the implementation effectiveness of the necessary environmental standards, norms, and regulations for the sector. The assessment would also cover the overall management mechanisms, including the institutional capacity of the sector agencies to address environmental and social issues, impacts and risks.

1.37 If the strategic environmental assessment reveals weaknesses, the government, all financiers and other key stakeholders would agree on a plan to reduce risk and enhance environmental sustainability, both at the program and sector level. In those cases where relying on the Borrower's system would pose a significant environmental and social risk, appropriate transitional measures to mitigate risk would be put in place while the Borrower's systems are strengthened.

3. Reviews, Monitoring and Evaluation

1.38 The sector program would be reviewed annually by the Bank, other participating development partners and the government. These joint reviews are the key instruments for evaluating the sector program, and would provide the main forum for discussing and resolving policy and operational issues, and for adjusting the sector program as needed. During the annual reviews, the results of the previous year's program would be examined and used as input in the next annual program. In addition, all parties would agree on numerous items regarding the next year's program, including: the activities to be financed, the expenditure plan, the procurement plan establishing method of procurement and the sources of funding, the resources each participant would contribute to the program, and the performance indicators to be tracked.

1.39 Prior to loan approval, the government, the Bank and all participating financiers would agree on a preliminary set of program output and, and when feasible, outcome indicators, and on the performance monitoring and reporting system to be used. To the extent possible, the monitoring and evaluation systems in place at the sectoral agencies would be used, and reinforced through the project if required. Progress on the agreed performance indicators would be assessed by all parties when the annual program of activities for the SWAp are reviewed. As a result of the project performance review, agreed-upon adjustments might need to be made to the operational plan or the sector policy framework. Typically in a SWAp, tracking program performance has been used to make adjustments to the project during implementation. However, in some cases it might be considered recommendable to attach some or all of the disbursements to project performance.

1.40 Finally, SWAps would follow all Bank requirements for monitoring and evaluation. It would require PPMRs and a PCR. In addition, as established in the Bank's ex-post evaluation policy, ex-post evaluations of SWAps would be done on a sample basis.

G. Evaluation of the SWAp Program

1.41 It is proposed that three years after the approval of this proposal, Management report to the Board on the implementation experience of Bank SWAps. In addition, six years after this proposal is approved, Management would deliver to the Board an evaluation of executed Bank SWAps and provide recommendations regarding future Bank use of the approach.

H. Exceptions to Bank Investment Loan Policies and Procedures

1.42 Bank participation in pooled funding will require some exceptions to Bank policies and procedures. First, Bank financing of eligible expenditures in the pooled account would not be restricted to goods, works and consulting services that comply with the Bank's requirement that the nationality of bidders and origin of goods be from member countries.

1.43 Second, goods, works and consulting services financed from the pool will follow national procurement rules and procedures, or other rules and procedures jointly agreed by all participants, provided they are governed by principles of economy, competition, transparency, publicity, equality and due process. This diverges from Bank procurement policy that requires that the procurement of consulting services follow the Bank's procedures and that goods and works below the threshold for international competitive bidding follow local legislation, provided it does not contravene Bank policies.

1.44 Third, supporting documentation for the individual transactions financed by the pool would not be submitted to the Bank for review. However, the Bank will be regularly provided with financial monitoring reports and audited financial monitoring reports for the entire SWAp program, thus permitting a review of the expenditures financed by the pooled account, and a verification that Bank financing fell below the total of eligible expenditures covered by the pool. In addition, the Borrower will be required to maintain adequate records of the transactions financed from the pool, and the Bank will reserve the right to request and review this documentation when deemed necessary.

1.45 Finally, the Bank requires that loan proceeds be placed in a special account and that the Borrower track the sources and uses of project funds. When participating in a pooled account, no special account will be created for Bank loan proceeds. In addition, given the nature of a pooled account, tracking the funds of each financier and identifying which financier financed which expenditures will not be possible.

I. Recommendations

1.46 Management recommends that the Board of Executive Directors approves the use of a sector-wide approach in investment loans, in accordance with the description of such approach contained in Sections F and H of this document and authorizes the President to enter into agreements with other development agencies for the purpose of participating in sector-wide approach programs under the terms and conditions set forth in this Document, by approving the proposed resolution attached hereto as Annex I.

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PROPOSED RESOLUTION DE-   /04

Sector-Wide Approach (SWAp)

The Board of Executive Directors

RESOLVES:

1. To authorize the use of a sector-wide approach in investment loans, in accordance with the description of such approach contained in Sections F and H of Document GN- ______.

2. To authorize the President of the Bank, or such representative as he shall designate to: (a) enter into agreements with other development agencies for the purpose of participating in sector-wide approach programs under the terms and conditions set forth in Document GN- ______; and (b) take any action necessary to give effect to such agreements.

DIFFERENCE BETWEEN SWAps AND TRADITIONAL INVESTMENT LOANS REGARDING FIDUCIARY ASPECTS		
	Traditional Investment Loans	**SWAp**
Scale	Usually includes a specific set of activities within one or more sectors.	Typically encompasses an entire sector, subsector or large portions of these.
Assessment of financial management and procurement capacity	Assessments focus on the executing agency responsible for executing the project.	Assessments focus on the sector institutions involved in executing the program. Assessments are jointly undertaken by financiers and results shared.
Rules and Procedures Involving use of funds	Standard Bank rules and procedures for financial management, procurement, and disbursements apply.	When funds are pooled, the government, Bank and other participating financiers agree on common financial management, procurement, and disbursement arrangements to follow. If conditions permit, country systems should be used. Financiers participating in the pool contribute to the pool in agreed proportions.
Use of Bank loan resources	Loan proceeds finance eligible expenditures which are verified by the Bank either ex ante or ex post by reviewing supporting documentation.	Loan proceeds forming part of a pooled account finance an agreed proportion of total pooled expenditures. Regular financial monitoring reports provided by the Borrower are used to verify that the amount of eligible expenditure in the pool exceeds the amount of Bank financing. Supporting documentation for individual transactions financed from the pool are not submitted to the Bank. The Borrower is required to maintain adequate records of these transactions, and the Bank reserves the right to request and review this documentation when deemed necessary.
Reporting and auditing	Borrowers provide customized financial and audit reports to the Bank on the use of project funds.	The government , Bank and all participating financiers agree on common reporting and auditing arrangements. To the extent possible, the government's systems are used.

DIFFERENCE BETWEEN SWAps AND TRADITIONAL INVESTMENT LOANS REGARDING FIDUCIARY ASPECTS		
	Traditional Investment Loans	**SWAp**
Procurement	If noncompliance with the Bank's procurement policies and procedures is declared regarding a Bank financed contract, the Bank's standard measures for noncompliance are applied to that contract.	If noncompliance, with the procurement procedures agreed among all parties, is declared for a contract financed by the pooled account, the Bank would reserve the right to cancel from its loan (or request reimbursement of) an amount equal to the value of the contract multiplied by the proportion of the pool financed by the Bank.
Expenditure eligibility	Eligibility for financing expenditures with the loan proceeds is determined by reviewing specific transactions.	The proportion of the pooled expenditures that are eligible for Bank financing is determined ex ante based on the program of activities and the procurement plan. The proportion of Bank financing to the pool is set below this proportion. At regular intervals the Bank verifies that the amounts contributed by the Bank to the pool actually fell below the eligible expenditures incurred, and that all expenditures financed from the pool formed part of the agreed expenditure program.

EXPERIENCE WITH SWAPS

Background

1. SWAps emerged in Africa in the 1990s as a result of a growing dissatisfaction with the traditional project approach which was viewed as fragmented, donor-driven, with high transaction costs for recipient countries and little impact on addressing development problems. The sheer number of donors and donor projects had overwhelmed governments with weak management capacity. Public sector expenditure had become an unplanned aggregation of donor projects lacking a coherent framework of policies, priorities and service standards. It became clear to both donors and the recipient countries that to increase the development impact of aid resources, all donor funding for a sector should support a single government-led sector strategy and expenditure program. In addition, transaction costs needed to be reduced by having donors align their preparation and implementation rules and procedures so that there could have joint programming, appraisal, monitoring and evaluation and move towards single fiduciary systems, and where possible, preferably those of the recipient country. This new focus led to the emergence of the SWAp.

2. Since their emergence, numerous SWAps have been financed primarily by the bilateral donor community, with some participation from the World Bank and the Regional Development Banks. There is no current data on the total number of SWAps that have been financed to date. The most recent data provides information until 2000. By 2000, a total of 78 SWAps had been financed in Africa, Asia and Latin America.[6] They were found exclusively in highly aid dependent countries. The majority (85%) were in Sub Saharan Africa, followed by Asia (12%) and Latin America (3%). Over half (56%) of the SWAps were concentrated in the health and education sectors and 17% in the transport sectors. The remaining SWAps were in agriculture, and a few in energy, environment, urban development and water.

World Bank Experience with SWAps

3. World Bank involvement with SWAps started in the mid 1990s. Historically, their SWAps have concentrated primarily in the social sectors and in countries with many donors. At year-end 2001, the World Bank had approved seven operations that reflected most fully the typical characteristics of a SWAp. Numerous other SWAps have been approved since then, however, the exact number is not known since, because it is an approach and not an instrument, there is no formal World Bank recording of SWAp loan approvals.

4. According to World Bank staff, however, demand for SWAps has notably grown in the last two years. In 2004 alone five substantial loans using the SWAp approach have been approved, with numerous others under preparation. Of the five SWAps approved, two where for Latin America and Caribbean (LAC).

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[6] Mick Foster, *New Approaches to Development Co-operation: What Can We Learn from Experience with Implementing Sector Wide Approaches?*, Overseas Development Council, London, UK, October 2000.

5. It is interesting to note that as the features of SWAps have evolved interest in the approach has extended to middle-income countries, particularly LAC countries. In 2002, the World Bank approved the first SWAp for a middle-income country (Brazil-Family Health Extension Project) and the first SWAp that contained pooled funding with the government. Since then, demand from middle-income countries has steadily increased. In 2004, SWAps were approved for Brazil, Mexico and Poland, with others under preparation.

6. The performance of World Bank SWAps generally compares favorably with that of the rest of their portfolio.[7] According to a review of SWAps done by the World Bank, as of June 2001 the execution ratings and development objective ratings were classified as satisfactory or better for six of the seven SWAps in execution. In addition, five of the seven operations had procurement ratings that were satisfactory or better, and there were no overdue audit reports for five of the seven projects.

7. The review did note that the cost and time it took to prepare and supervise these SWAps were significantly above the average for the rest of the portfolio. Overall, the average cost of preparation and supervision was more than double that of the World Bank average. In addition, the average time it took from preparation to Board approval was also double the Banks average. The high cost involved in the preparation and supervision of these SWAps was the result of the large number of donors that needed to be coordinated and harmonized and the weak local capacity. In middle income countries with stronger local capacity and no donor participation, the time and cost of preparing and supervising a SWAp would not be expected to vary from that of the average investment loan. In addition, once a SWAp is established for a sector in a donor dependant country, the preparation and supervision costs of subsequent SWAp operations in that sector should be substantially reduced.

[7] *Fiduciary Arrangements for Sector Wide Approaches*, World Bank, April 2002