

A Draft Report

**REPORT ON FINANCIAL MODALITIES AND FUNDS FLOW
FOR DANIDA APPRISAL OF
FUTURE SECTOR SUPPORT TO SECONDARY EDUCATION
DEVELOPMENT IN NEPAL**

A Comparative Assesment between HMG/N, WB, ADB and Danida

Presented to

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Preface

The observation of Nepal's development efforts since last couple of decades reveal that a significantly large portion of development budget is comprised of bilateral and multilateral grants and loans. The importance of foreign source of fund in the development initiatives in Nepal, need not to be over emphasized. Number of funding agencies involved in different sectors in numerous project. However; they have their own funding modalities, procurement guidelines, accounting, reporting, internal control and auditing requirements. Therefore, a harmonised system is imperative.

Secondary Education Support Program is designed to implement in 10 districts at a time with the funds from various sources. The study team has to assess the procurement, disbursement, reporting and auditing requirements of various funding agencies in a given time frame so that a harmonised financial administration system could be introduced in the program. It has also to look upon the basket funding model adopted in BPEP II.

The report is presented in seven different chapters. The first chapter is introduction about the study; the second chapter gives a very brief status of secondary education in Nepal and ; the third chapter is related to decentralization. The third chapter highlights the authority and responsibility of LGIs, particularly DDC/VDC, which are supposed to involve in education service delivery. The funds flow mechanism and reporting/auditing mechanisms for DDF are just traced out. From fourth chapter onwards, we have focussed on requirements on accounting, procurement, auditing and reporting by donor agencies viz a viz HMG/N, analysis of basket fundings and finally findings and recommendation.

We would like to express our sincere thanks to the BPEP II PAT for giving us this opportunity. We will be more than happy if the report can be any help to make the funds flow smooth and to harmonise the accounting and reporting system in the proposed secondary education-support program.

Finally, we would like to express our sincere thanks to the persons from governments and donor agencies who have provided their time and valuable information for the study. Mr.Suman Adhikari and Ms.Kamakshi including BPEP II, Danida PAT office staff deserve special thank for their every support during out study.

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I. INTRODUCTION

A. Background:

1. A recently developed Secondary Education Development Plan under ADB technical assistance has identified four strategic goals of secondary education development in Nepal as:
 - (a) to enhance the quality
 - (b) to ensure equitable access
 - (c) to promote the relevance of secondary education to national development
 - (d) to enhance both external and internal efficiency

2. Further to expand the quality secondary education suitable for the need of national development – Secondary Education Support Program (SESP) has been developed Jointly by HMG/N, the ADB and Danida. The SESP was based on 10th five-year Plan, Medium Term Expenditure Framework, Local Self-government Act (1999), Education Act (7th amendment-2002), and SEDP. SESP has the main objectives to improve the quality of public secondary schools; to improve access to public secondary schools particularly for girls students with disabilities and students from poor and disadvantaged groups and to develop the institutional capacity of central and local governments and local communities to sustain and deepen the school improvement processes.

3. **On the basis of above objectives a joint programme between HMG, ADB and DANIDA was undertaken for future support to secondary education for coming five years. The programme document has outlined a number of options with respect to financial modalities and mechanisms including basket mechanism adopted in BPEP II. In order to promote coherence on the part of donor involvement (ADB and DANIDA with HMG) in the secondary education and possible involvement of other donors in future the rules, regulation and financial requirements of HMG/N, ADB, World Bank and DANIDA need to be compared. This study was designed particularly to address the need relating to financial modalities in SESP.**

4. This report presents the outcome of a review of financial modalities and mechanism followed by ADB and DANIDA in project funding/loan and grant assistance to Nepal viz a viz financial modalities and practices adopted in BPEP II, a basket funding mechanism. The review is an integral part of SEDP appraisal mission, and this study has been commissioned by BPEP II, DANID Programme Advisory Team. Proposed SESP is a multi-donor development project, therefore, warrants procedurally compatible to a maximum extent to each others, standard and simple to understand and to follow by the executing agency and reasonably acceptable to all the funding agencies not exclusively include HMG/N, ADB and DANIDA.

B. Scope and Objective of the Study

5. The SESP has outlined the following four possible approaches to programme funding:
 - ? To use the existing BPEP basket approaches (Core Investment Programme) and expand it to cover primary and secondary education.
 - ? To develop a separate basket funding for secondary but working in exactly the same way as BPEP II
 - ? To use a parallel funding modality based on using existing Danida and ADB modalities
 - ? To develop a hybrid approach using a mixture of parallel funding, and a common account, but different from the procedures used in BPEP

With reference to the above mentioned alternatives this study has to

- appraise the ADB financial procedures for loan funds to a project and implication of the agreement for programme funding to other funding agencies
- appraise possibility for DANIDA direct funding in tune with the government reform process in the field of decentralisation, particularly financial decentralisation
- assess that fund flow, reporting and auditing requirements with integration into the HMG system between donor funding to SESP and the national budget
- compare financial requirements, rules and regulation of HMG, ADB, World Bank and DANIDA

(TOR for Appraisal mission is attached)

The review team has carried out the following tasks

- Reviewed the documentation collected by DANIDA – PAT office
 - Supplementary discussion were held with the FCGO officials, finance officers in DOE and MOES, DASU and concerned officials in ADB and World Bank
- Frequent interactions were held with DANIDA – PAT office as and when required.

C. Methodology:

6. Basically this is a desk study. However, a few in house discussions and interactions were held with concerned staff in government offices as well as in donor agencies. It has been observed during preliminary review of the available documents that DANIDA, ADB and HMG agreed in principal to follow a basket funding mechanism as already adopted in BPEP II. But DOE has been facing some challenges to implement the basket funding system and the funding agencies are also not sure that funds are reaching to the beneficiaries in time through this process. Therefore, the focus of the study was on reviewing the barriers and bottlenecks of the basket system in BPEP II. Funding modalities, reporting, documentation and procurement guidelines of HMG/N, World Bank, ADB, and DANIDA were also reviewed separately and compared to each other for their compatibility as well as differences. While assessing the funds flow mechanism provisions in the Local Self-Government Act, 1999 and the Seventh Amendment in Education Act were also considered. This is a desk study therefore a detailed field survey to collect primary source of information was out of scope. The report is based on secondary source of information and information collected during the in-house interactions with a few concerned.

II. SECONDARY EDUCATION IN NEPAL

A. General Information

7. Secondary Education is a sub-system of the Education System in Nepal. It consists of lower secondary (grade 6-8), secondary (grade 8-10) and higher secondary (grade 11-12). The lower and secondary (from grade 6 to grade 10) levels of education have been identified as the main area of concern for the Sector Support Program for Secondary Education. A very brief outline of secondary education in Nepal is given in following paragraphs.

8. Enrolment in secondary level is increased dramatically in the past two decades. However, net enrolment ratio at lower secondary and secondary level is 31% and 21% respectively. The number of students at lower secondary and secondary level in the year 2000/01 academic year is 988826 and 427733 respectively. The number of teachers at respective level is 25794 and 20051. Similarly, the number of schools in lower secondary is 7710 and in secondary is 4488. Student teacher ratio is 38 in lower secondary and 22 in secondary level. Out of 4488 secondary and 7710 lower secondary schools, 3022 are private secondary schools and 4029 are

private lower secondary schools. Accordingly, student teacher ratio is 24 in lower secondary level private schools and 14 in private secondary schools. Approximately 33% in lower secondary and 50% in secondary level teachers are trained. There is a considerable variation in school attainment by gender, socio-economic groups, by regions as well as by ecological zones. Due to quality perception, generally measured by SLC results, attraction is considerably growing towards private schools in urban and semi-urban areas. This phenomenon has further aggravated accessibility problem of poor and disadvantaged in quality education

9. A World Bank Sector Review (2001), a MOES, Danida analysis on the secondary education (2001), a high level committee formed by the government (2001), and Secondary Education Development Plan Document (2001) all have invariably pointed out a number of problems in education system. Challenges identified in those reports not exclusively include low levels of literacy and educational attainment, unequal participation in schooling across income groups and social groups, high repetition and dropout rates through out the system, and low quality of education that does not serve the labour market well. A few problems, among others, are highly politicised but poorly trained/under qualified teachers, obsolete but overloaded curriculum, lack of proper support of the community to the school, improper distribution of public resources, etc.

Based on the problems as identified the Secondary Education Support Program has been developed by HMG/N, the Asian Development Bank (ADB) and DANIDA, to provide that overhaul and expand quality public secondary education. Initially the program will be launched in 10 districts on a pilot basis from January 2003 for five years period.

10. HMG/N, MOES has been working closely with existing and new development partners in SESP to harmonise funding modalities and increase the capacity of the government to manage fund while at the same time improving the flow of funds to enable the program to meet its objective. This study is also aimed at achieving the a/m objective.

B. Components of SESP

11. SESP has outlined the following component in ten selected districts for coming five years to be implemented

Component One-The Learning Environment: This component, not exclusively, covers the activities as refurbishment, maintenance, rehabilitation of physical facilities and expansion of secondary education ensuring better access to poor, disadvantaged and women. It is obviously observed that most of the activities are to be held at local level.

Component Two-Curriculum Development, Assessment and Instructional Materials: This component covers teacher's training and curriculum development fora at sub-district, district and national level. Development of teaching aids, instructional material and text books are also incorporated within this component. Strengthening RED to enable it to conduct SLC examination is also one of the core activities under this component. As we see the nature of the activities to be conducted under this component central level and regional level institutions have to play a major role. Where as some of the activities are to be conducted at district, sub-district level and local level as well.

Component three-Teacher Evaluation and Development: This component includes, not exclusively, the activities as demand driven teacher training, improving in recruiting female teachers, developing master trainers, strengthening the policy formulation mechanism, provision of NCTD, accreditation of teacher training campuses etc. The involvement of community level organisations like SMCs/schools, district level organisations and central level organisations seems apparent to implement those activities.

Component Four- Institutional Management and Capacity Building: This component incorporates the activities like management improvement at school level, district level, regional level and central level. Human resource Development, Organisational Structure at Central Level, Provision for Information/communication and School Supervision are the other activities incorporated in this component.

III. OTHER RELEVANT REPORTS TO THE STUDY

A. The MTEF and 10th Plan

12. The Medium Term Expenditure Framework for the first three years of the 10th plan period has been developed with the primary objective of improving the fiscal management of the government. The Ministry of Education and Sports, along with other four ministries, was also chosen for this analysis. The MTEF exercise has analysed the development budget and expenditure of the concerned ministries. It has also categorised the expenses for coming three years into priority one, priority two and priority three. The Secondary education is under priority second where as basic and primary education is on the top. MTEF has forecasted the development budget for coming three years in which the allocation for proposed SEDP has also been considered to 21%.

13. Tenth development plan (2002-2007) approach paper focuses on to increased community participation and mobilisation in managing and resourcing at school level. It also emphasises on decentralisation of education management, planning and monitoring. Cost sharing in secondary education (government funds, local resources, fees with scholarships) and planning and implementation of school based management/development systems are the other dimensions emphasized in the 10th plan approach paper to enhance the quality as well as access on education.

Proposed sub-sector budget allocation for coming three years

	Proposed
Basic and Primary Education	53%
Child Development & Pre-primary	5%
Non-formal Education	2%
Secondary Education	21%
Technical & Vocational Education	2%
Higher Secondary Education	2%
Higher Education	15%

Source: MTEF, Education Sector (2002/3 – 2004/5)

1.1. IV. DECENTRALIZATION AND LOCAL SELF GOVERNANCE

A. Objectives and Rationales

14. Local Self Governance Act, 1999 was enacted with basically following four objectives:
- ◆ to make provision conducive to the enjoyment of the fruits of democracy through the utmost participation of the sovereign people in the process of governance by way of decentralisation,
 - ◆ to institutionalise the process of development by enhancing the participation of all the people including the ethnic communities, indigenous people and down-trodden as well as socially and economically backward groups in bringing out social equality in mobilising and allocating means for the development of their own region and in the balanced and equal distribution of the fruits of development,
 - ◆ to have institutional development of local bodies capable of bearing responsibility, by providing such responsibility and power at the local level as is necessary to formulate and carry out plans, and
 - ◆ to constitute local bodies for the development of the local self-governance system in a manner that they are able to make decisions on the matters affecting the day-to-day needs and lives of the people, by developing local leaderships

15. In pursuance of the above objectives, following principles and policies for the development of local self governance are as followed:

- ◆ Devolution of such powers, responsibilities, and means and resources as are required to make the Local Bodies capable and efficient in local self-governance.
- ◆ Building and development of institutional mechanism and functional structure in Local Bodies capable of considering for local people and bearing responsibilities.
- ◆ Devolution of powers to collect and mobilise such means and resources as are required to discharge the functions, duties, responsibility and accountability conferred to the Local Bodies.
- ◆ Having the Local Bodies oriented towards establishing the civil society based on democratic process, transparent practice, public accountability, and people's participation, in carrying out the functions devolved on them.
- ◆ For the purpose of developing local leadership, arrangement of effective mechanism to make the Local Body accountable to the people in its own areas.
- ◆ Encouraging the private sector to participate in local self-governance in the task of providing basic services for sustainable development.

B. Village Development Committee (VDC)

16. VDC is the smallest unit of the local self government, constituted by the elected chairperson, vice chairman, nine ward chairperson and two members including one women nominated by the village development committee. This is an executive body and performs local development activities as per the programs and budget approved by the Village Council. The council is the supreme body comprised of 45 members – 5 from each 9 wards including Ward chairperson, VDC chair and vice chair, two nominated members.

17. VDC has, not exclusively, following Functions, Duties and Powers relating to Education

- ◆ to establish pre-primary schools or to give permission to operate
- ◆ to supervise and manage the schools being operated within the village
- ◆ to assist in providing primary level education in mother tongue
- ◆ to make programs on adult education
- ◆ to make arrangements for providing scholarships to the students of oppressed ethnic communities; and
- ◆ to conduct other various activities on sports, library, women development, human resource development, protection of orphan, disabled etc.

Planning Process at VDC:

18. A village development committee shall have to formulate periodic and annual plan considering six priority areas including projects contributing, among others, to the alleviation of poverty, projects having large people participation, and providing direct benefits to the women as well as backward class children. VDC obtains guidance and prior estimation of resources from the DDC by 15th December and collects projects from Wards, NGO, CBOs, and Users' committees. Project are to be selected based on socio-economic analysis, resource mapping and feasibility study. Taxes, services charges, fees, loans, grants and other incomes are the sources of funds. Provision of public hearing and auditing committee for internal control mechanism is devised. Registered auditor approved by DDC and nominated by Village Council has to conduct external audit. The audit report has to present in Village Council. However internal audits are conducted by DDC on trimester basis.

1.1.1. District Development Committee

19. DDC is the largest Unit of Local Self government constituted by the elected members by the municipal councils and village councils of the district from amongst themselves at the rate of one member from each area. Similarly, one president and vice-president are also elected in a district amongst themselves. Members of the House of Representatives and the National Assembly within the District and two members, including one woman, nominated by the DDC are also the member of the DDC.

20. Functions, Duties and Powers of DDC relating to Education

- ◆ to set priority for establishing schools
- ◆ to make recommendation, set out rationale and reasons for the approval and dissolution of the schools
- ◆ to supervise, monitor and assist the schools in their operation and management
- ◆ to formulate adult/informal education plan

DDC may give grants for the approved program to any organisation, association or body being subject to the approved budget. However without prior approval of HMG a DDC cannot enter into agreement with any international non-governmental organisation or foreigner for the purpose of accepting grants.

District Development Plan

21. A district development committee shall have to formulate periodic and annual plan considering priorities including projects contributing, among others, to the district level policies and goals, overall necessities indicated by the periodic plans, plans received from VCs and Municipal Council and directives received from the NPC and concerned Ministry on national development policy. DDC obtains directives and prior estimation of resources from NPC and Sectoral Ministries by 15th November. Prior to formulating the annual plan the DDC has to prepare an estimation of sources and means. Projects are to be selected based on socio-economic analysis, resource mapping, feasibility study, contributing to the protection and promotion of the environment, and which may have utmost participation of the local people and labour.

Fund of the District Development Committee

22. Amount received from the Government; amount raised from taxes, services charges, and fees; amount received as loans, donations and grants; amount obtained from sale, lease, fare or interest of movable and immovable properties; amount obtained from income generating programmes; amount obtained from any foreign government and international organisation; amount received from revenue allocation (presently 25% of the land revenue goes to DDF), fines, penalties and other incomes constitute a fund of the DDC. However, prior to obtaining the amount from foreign government and organisation DDC have to obtain prior approval of HMG/N. Provision of auditing committee within DDC for internal control mechanism are devised in the expenditure done from the fund. The AGO itself has to conduct external audit. The audit report has to be present in account committee and District Council.

23. Planning, Implementation and Monitoring of a Project from DDF

1. Ensure the Availability of Fund, Priority, Guidelines from centre and Feasibility of the project under consideration
2. Plan Program and Budget Approved by District Council
3. Work Plan Prepared by DDC
4. Monitoring and supervision team constituted
5. Project implemented expenses incurred are paid from an operating account. The required amount for the project is to be transferred to operating account. The DDF is operated with the signature of Secretary and financial administration chief, expenses are approved by DDC, chair person/secretary as authorised by the regulation.
6. Internal auditing is done by DDC and external by AGO or designated
7. Reporting to DDC and ultimately to DC which, sits twice a year normally
8. Audit committee formed with a chair of one of the DDC members and report of audit committee as well as auditor are presented to District Council.
9. Co-ordination is required with the sectoral office to check the duplication
10. Funds from DDF are to be expended as per the district development plans. The provision of supervision and monitoring from DDC members is also provisioned in the LGA. The release of fund from DDF goes directly to the expending account DC is the sole and supreme authority for this fund where as the DDC play a central role to execute the programme from the fund.

C. Provisions Regarding Users' Committee

24. The projects to be operated at the local level with a costing up to 2.5 million rupees shall be given priority to be carried out through the Users' Committee formed by the local users. But DDC can decide to give a work valued more than one million rupees to users' committee. DDC has to provide technical support to the users' committee if the construction work is awarded to it.

An agreement has to be signed between the users' committee and the DDC stating the portion of the people participation out of the total cost of the project which amount is not supposed to finance by the DDC. Users' committee is not allowed the work to be carried out through contractor. After completion of a work the responsibility of repair and maintenance lies on the users' committee. After completion of the project the project should be handed over to the users' committee. The users' committees are authorised to charge fees from the users to operate and maintain the project.

25. Local self-government Act has empowered the DDCs, Municipalities and VDCs, which grants significant powers and responsibilities to run local services including education. The Government, in principle, is committed to a decentralised governance system. However, while drafting sectoral legislation it has been observed a number of inconsistencies with the LSGA. The recent phenomenon is the 7th Amendment in Education Act, which also is not in alignment with LSGA. However, the Act has introduced the teacher licensing system and opened the avenues for the active involvement of stakeholders in school management.

26. FCGO and DOE officials reported, during discussions with the study team, that from the coming fiscal year onwards warrants (authorisation to expend) for salaries of the teachers at primary level and other recurrent expenses in BPEP II are going to be issued to DDC directly. The process is yet to finalise before put into action. This is a step ahead in decentralisation path if implemented in a spirit of devolution. However, a significantly large portion of program allocation will go to DEO's account and will be continued in the future as well. The main stress of the Education Act (7th Amendment) is on returning the schools to the community. At present time it is difficult to determine the precise arrangement in a given context of differences in legislation. However; accountability and responsibility of SMCs, VECs, DEC, DDCs and DEOs need to be clarified before launching any programme. Similarly, flow of funds and the accountabilities to the outputs as well as reporting are to be determined.

D. Public Expenditure Review Commission

27. A public expenditure review commission was formed in the year 2000. The Commission has assessed the performance of different organisations, role of private sector and local governments, viz a viz government and tried to locate the mismanagement of precious resources. This document clearly spelled out to transfer the primary and lower secondary education to the VDCs and secondary education to DDCs. The Commission recommends the government to provide a block grant to VDCs and DDCs equals to the current budget and suggests to review such block amount based on certain indicator on a certain interval of time. The provisions in the report are still not incorporated in sectoral legislation.

V. BUDGETING ACCOUNTING AND PROCUREMENT

A. His Majesty's Government of Nepal

Budgeting

28. Budgeting, procurement and accounting practices are governed by the Financial Procedures Act 2053 (1998) and the Regulation Relating to Financial Procedures 2056(1999). Annual Budget (16th of July - 15th of July) is prepared by each line ministry as per the budget manual and guidelines. All types of proposed revenues, domestic borrowings and foreign aid

(loans and grants) is required to be incorporated in annual budget. The budget is presented to the parliament each year. Proposed expenses for coming fiscal year with the progress of current year is tabled in the parliament as an Appropriation Bill. The parliament passes the Bill and forwards to the HM King for royal seal. After royal seal the budget for a year is approved. If the budget is not approved on the first day of the fiscal year, Advance Appropriation Bill is passed to authorise the Government to spend up to one third of the total of appropriation bill. Once the budget is approved, Ministry of Finance (MOF) issues warrants to all the line Ministries with total amount of budget desegregated by source of funding and guidelines for expenditure. Under certain circumstances the MOF has right to control over it. All the line Ministries has also to forward warrants with guidelines for expenditure to the respective Departments and ultimately from Departments to the respective expending units. Normally expending units are executing bodies located at district level.

Disbursement

29. At the beginning of each fiscal year one sixth of the total expenses incurred last year (sometime it is recurrent only) is released from District Treasury Controller Office to each expending units on reimbursement basis. In addition to this, government is planning to implement a new release system for priority one projects from coming fiscal year. In this system instead of usual 1/6, one third of total budget is to be released in the initial imprest account so that the projects would not be running out of fund at any time. Secondary education is a priority second project therefore would not be effected from this system at-least for coming f/y. However, in order not to hamper the development projects there is a provision of additional imprest amount to be released over and above of usual 1/6 of total budget. The amount is agreed upon the mutual consent between the DTCO and respective spending unit. Funds for a foreign aided project is released from DTCOs after verifying the lists of offices having Release Suspension Order received from FCGO. Budget release suspension order is issued by FCGO to all district treasuries on the advice of MOF after the commencement of new fiscal year. Basically, following two criteria, normally, apply for the suspension of the accounts. 1) If the source provided for in the budget is such that there is no firm commitment or no agreement has yet been signed, and 2) If there is a huge balance of outstanding to obtain reimbursement from the donors. Financial Controller General Office (FCGO) releases open order when it receives a confirmation from MoF about the certainty of donor funds or when it finds donor reimbursement is deposited in the central treasury either from pre-funding or from replenishment. All the expending units have to submit monthly statement of expenditures, advances, bank statement (reconciled) and physical progress to the respective DTCO to get reimbursement on a monthly basis. The executing units also submit the statements of expenditures with progress report in a prescribed format to either the respective Departments or the Ministry which ever is applicable.

30. A separate bank account called a special account or an imprest account is maintained by the donor-funded projects. If the donor's fund is pre-funding certain amount is deposited to the central treasury at the beginning of the year and replenished as and when required. If it is a loan or a grant on reimbursement basis the expending unit expends as per the budget and guidelines and submits the accounts to the respective Department or the Project Implementation Unit (PIU) at centre. PIU collects the accounts from the districts, consolidates, verifies the authenticity of the expenses, transfers the same amount from imprest account to the central treasury. Similarly, the PIU submits the withdrawal application to the funding agency. Once it is approved replenishment takes place at the special/imprest account. Any unspent amount at the cost centre's account is withdrawn to DTCOs at the end of each fiscal year. A grant to the Village Development Committees and District Development Committees are released from respective DTCO on trimester basis when warrants are reached to the DDCs and DTCOs from the Ministry of Local Development. Any unused funds have to remain with DDCs and VDCs funds in principle. But as per the budget speech of F/Y 2001/02 those two grants are also frozen at the end of each fiscal

year. For program/project grants the spending institution is authorised to claim up to total budgeted amount. The transfer of the funds is due on a reimbursement basis. Any unutilised fund is frozen.

Accounting

31. Accounting is maintained on cash basis. Every income, loans and grants are directed to the Treasury of Government and the usage of resources is appropriated through the budget. Budgets are broken down into budget heads and expenditure line items. Actual expenditure by program component or activity is not required to maintain. Although, as per the Regulation Relating to Financial Administration, 2000 each expending unit has to prepare and submit a physical progress report to DTCO each month this provision is not fully complied till now. If there is any specific reporting format required as per the agreement with funding agency, and the normal accounting is not sufficient to provide the required information, a subsidiary books of account is maintained at each spending unit level. The system of keeping subsidiary ledger is invariably applies in the projects where category wise reporting is required to get replenishment.

Procurement

32. Normally, internationally accepted practices and procedures are followed in procurement. Separate provisions for procurement of goods and services are in place. Procurements are done directly, or through local bidding or global tenders.

Internal Control System

33. Competent Authority while sanctioning government expenditure must pay attention to 18 specific items from the viewpoint of regularity, economy, efficiency, effectiveness and propriety. S/he should be confident enough of accuracy and correctness of the documents presented for the expenses from the coffer. Competent Authority should insure that the internal control system is sufficiently enough to prevent loss of, damage to, and misuse of cash and goods and other government property as well. Sanctioning process covers the authorisation, verification of approval, check and balance procedures for budget operation, approval/sanctions, implementation and monitoring. Foreign aid management and accounting; assets/inventory management accounting and reporting; execution of procurement and public works contracts; verification of work completion report; revenue and expenditure accounting; conduction of internal auditing, preparation of statement and reporting and the settlement of irregularities are the duties and responsibilities assigned to a competent authority. Payment of bill is made only by the approval of competent authority and Bank accounts are operated with a joint signature of authorised person and accountants. Internal auditing is done by DTCO.

34. There is a provision for Separate Accounting Cadres supervised by FCGO. The FCGO conducts all administrative activities related to the administration of Account Cadres. There is a special provision in financial regulation that an accountant can give different opinion or disagree with the project/department chief on any payment that an accountant feels that the transaction is not followed with the procedures prescribed in Financial Administration Regulations/ or other regulations related to finance. Accountants are conferred with this to maintain a sound internal control system.

Auditing

35. Auditor General Office, a statutory body, is empowered by the constitution of the Kingdom of Nepal, 1990 and has every right to access on public financial transactions and is a

sole authority to conduct external audit of all public budget and accounts. Respective DTCO conducts internal audit on each trimester basis and external auditing is done by the Auditor General Office once a year. External auditor covers district level government offices, DDcs, and Government Projects. Accounts of Schools and VDCs are done by registered auditors.

B. DANIDA

General guidelines for Accounting, Documentation, Auditing and Reporting for recipients of Danish bilateral development assistance

36. Denmark believes in the principle of full integration of external assistance into the appropriate national structure. Preferably, external funding, including contribution to the private sector should be channelled through appropriate government system. Danida wants to ensure detail arguments for a chosen level of transfer of fund, accountability and responsibility to the co-operation partners, financial flow procedures (frequency, responsibility, modality), accounting and internal control procedures and auditing procedures for any sector support. Organisational structure including financial management and control, description of anticipated cash flow system and MIS are also considered while providing grant assistance.

37. It has to be ensured that sufficient documentation on the previously paid instalments have been spent in accordance with the agreement. The documents should also ensure that grant is spent in accordance with the accepted budget limits. Reporting must include satisfactory accounting and auditing for all income and expenditure preferably linked into activities and sector strategic performance indicator. Overall progress report of all activities must be submitted once a year or as per the agreement. Danida is entitled to have access on all relevant information and inspection any time during the period covered by the agreement.

38. Use of Danish grant should be appropriately accounted and accounts of implemented activities should be submitted within six months after the expiry of the fiscal year under review. All accounts must be accounted by the competent control authority of the recipient country and endorsed by auditors and comment if any. Danish auditor should be allowed to study report. Grants are paid in advance to the recipient country. Audited accounts should be submitted in pursuance of Danida's General Guidelines for Accounting, Reporting, and Auditing. In addition to all the activities stipulated in the budget are to be reflected in the accounting.

Procurement Rules and Guidelines- Goods

39. Local procurement shall in addition to Danida's guidelines – follow the legislation of the recipient country and practice which is not contrary to the legislation of Danida.

Amount	Minimum Required number of tenders	Methods of bidding	Call for Tender
Up to 50000 DKK	1	Direct request	By letter
From 50000 DKK to 1m	2 - 3	Invited tenders without advertising	By letter
1m to 3m Dkk	3 – 5	Pre-qualification without advertising	By letter
- 3m Dkk and above	3 – 5	Pre-qualification followed by invitation of bid	By advertising

In principle, procurement in the developing countries follows Danish legislation unless local legislation is detailed enough but it should appear in the agreement.

40. Danida's procurement agreement is based on Standard Bidding Document of Goods, May 1993 of World Bank. The tender should clearly contain the specification of need of supply, content of bids and invitation to tenders with name, quantity, quality of the required article along with the time of delivery, terms of delivery, terms of payment etc. Evaluation of tenders is made based on financial implications but one should also ensure that the terms and conditions are also met. There is a specific Danida's procurement guideline, which also clearly states the specification of the supply of goods as well as bid evaluation criteria.

C. Asian Development Bank (ADB)

41. Banks disburse the fund in following ways

- (1) Direct payment
- (2) Commitment
- (3) Reimbursement
- (4) Imprest fund

42. Followings modalities of procurement are generally followed in ADB funded projects:

- ? International Competitive Bidding
 - ? two stage bidding
 - ? second stage price proposal
 - ? international shopping where the amount of the contract is not much large
 - ? local competitive bidding
 - ? community participation in procurement as outlined in each agreement.
- Pre-qualification procedures

Accounting and Auditing

43. Bank requires adequate records consistently maintained in accordance with generally accepted accounting principles by competent personnel and audited in accordance with auditing standards and available for review by Bank. To the extent possible account are to be maintained in accordance with International Accounting Standard. Auditing should be done by a qualified and independent auditor with a written opinion as to the extent to which financial statements, can be relied upon. Auditing requirements of the Bank include the auditors' view on compliance of loan covenants, financial statement of expenditure, financial controls and management systems. Bank also accepts audited financial statements prepared on the basis of generally accepted local accounting standards, provided that the important differences are disclosed therein. Bank may requests to the recipient to prepare a supplementary information that may be different from those generally required by local accounting practices.

44. Accumulated transaction up to a particular year is also required to be reported with periodic financial report. Auditing is required to be done with International Auditing guidelines. Normally, the Bank accepts the government auditor if the auditing authority is a statutory body. Frequency of reporting will be based on project/programme agreement. Generally, interim statement within one month of the close of reporting period; unaudited annual statement within the three months of close of each fiscal year and audited accounts within six month of close of each fiscal year are to be submitted. The bank reserves the right to inspect and review the project accounts financed by its fund. There is a detail guidelines for procurement and disbursement. Specific formats for recording, reporting and reimbursement are designed and enforced.

Ineligible Expenses

45. Bank has specified certain expenses that are ineligible for finance under Bank loan. Those items among others are taxes and duties, cost of land acquisition or right of way, working capital (other than incremental and initial working capital), interest and charges other than those on Bank loans, and expenditure not directly connected to the Bank financial projects.

D. World Bank

46. Procurements and funding mechanisms in ADB and World Bank are almost same. Following modalities of procurement are normally followed in World Bank funded projects:

- International Competitive Bidding
- Two stage bidding
- Modified ICB
- Limited International Bidding
- National Competitive Bidding
- Shopping (International and National)
- Direct Contracting
- Force Account
- Procurement from UN Agencies

47. In a World Bank funded project there is an extensive framework for financial monitoring and auditing. Financial accountability assessment by WB is done both for the country specific and the project specific. Reporting and auditing requirements for the bank are determined based on the level of risk and complexity of the project. International Accounting Guidelines and INTOSAI Auditing Guidelines are acceptable to the bank. In the same way the Bank may inspect and review accounts of a project financed by it.

A consolidated chart of comparative Procurement Provisions and a comparative chart showing planning, accounting, auditing, and reporting is annexed. Fund flow showing different modalities flow chart of fund and reporting are also annexed.

VI. A BASKET FUNDING MECHANISM

A. Basic and Primary Education Programme

48. The funding to the Basic and Primary Education Programme includes the development and recurrent budgets anticipated for Basic and Primary Education for the five years period which started in fiscal year 1999/2000. The programmes are broken down into following four parts.

- The Core Investment Programmes (CIP)
- Non-core development programmes funded by the other donors
- Non-core development programmes funded by HMG.
- Non-core regular programmes funded by HMG.

49. A basket funding modality has been chosen for funding the Core Investment Programme. Danida, European Commission (EC), Finland, Norad, IDA (The World Bank) and the HMG/N together provide fund in a basket. The non-core development programmes are financed by JICA, UNICEF, ADB, where as HMG would fund core as well as other non-core development programmes and regular programmes. The financial procedures set for the operation of basket fund involves the followings:

- ◆ Pre-funding of all local currency expenses is made by HMG for local payments.
- ◆ All the donors deposit initial amount as pre-funding in special accounts of each donor.
- ◆ **Direct payments is made to the suppliers abroad from special accounts**
- ◆ Withdrawal of loan or grants proceeds is ensured from the donors accounts as per the approved expenses
- ◆ A comprehensive record keeping and reporting is imperative
- ◆ Preparation and submission of preliminary project accounts as well as audited project accounts within the stipulated time frame.
- ◆ As the payments in local currencies of donor's share is pre-financed by HMG, the project would compile the expenditure with payments details from the cost centres (all the 95 cost centres), segregates the share of expenditures to each donor as per the credit/grant agreement to reimburse such pre-funding.
- ◆ Transfer the exact or eligible sums to HMG treasury account debiting the World Bank's special account and donors account.
- ◆ Submit withdrawal application to the World Bank for replenishment to the special account.
- ◆ As soon as replenishment occurs, transfer the exact or eligible sums to HMG treasury account debiting the corresponding special accounts of other donors as well.
- ◆ Request other donors to deposit the amount as and when required according to planned budget/expenditure.

B. Accounting and Reporting Procedures

50. The release of funds to the District Education Offices and other Central Offices including Department of Education is made through the District Treasury Controller's Offices, located in each district. The amount released is equivalent to two months expenses at the beginning of the year and replenishment will occur each month based on the statement of expenditure submitted to the respective DTCO.

51. While keeping accounts and disbursements World Bank project accounting and disbursement procedure are followed. In this procedure, the funds from each donor would initially be routed to Special Accounts, which will be used for reimbursements to HMG against the donor's share of local expenditure or the payment to be made in foreign currencies (direct payment to the supplier from special account). The DOE needs to send statement of expenditure (SOEs) in the prescribed format as per the World Bank disbursement categories to the World Bank for replenishment. The Department has to consolidate the project expenditure by source based on the monthly statement of expenditures and supplementary details of payments (SOEs) forwarded to the DOE from the districts, and thereby rearrange the budget items under each expenditure category. The DOE would maintain project account based on the expenditure reported by the cost centres, whereas the supporting documents related to the transactions would still be retained at the respective cost centres.

C. **Problem identified/Lesson learned.**

52. The expenditure code of HMG accounting system does not directly correspond to disbursement categories. So each cost centre has to rearrange the expenses in an item-wise expenditure sub-ledger and has to report accordingly. Although the funding modality is termed

as basket funding district level accountants have to maintain numerous subsidiary books. Generally district level staff are not competent enough to maintain a complex system. Unified accounting and procurement system introduced through basket mechanism has certainly simplified the process at district level but there is a scope to modify the modality to make it more simple and effective.

53. Budget sub-heads 65-4-411 (Central level) and 65-5-411 (District level) have been prescribed for BPEP II. Actually, these budget sub-heads should have been meant only for CIP main basket. Yet it was found in the first two years of the programme that these allotments were diverted to pay the salaries to a number of Female Teachers and Resource Persons that fall under the recurrent liability of the government. It caused a confusion and considerable delay in disbursement. Also, the budget for UNICEF activities, which is non-cip, is included in budget head 65-4-411. Resultantly, it increased the accounting function of the DEO's and the Department, as they would need to maintain separate set of accounts under each budget sub-heads i.e. 65-4-411 and 65-5-411. Consequently, accounting process for both at the cost centres and the Department of Education has turned to be quite complicated.

54. By definition of HMG budget item no. 3.02, (other grants) should include only the grants to schools. But in practice the budget for different activities under education programme are also allocated in this line item. So it is quite complicated to scrutinise the Training, Grants, Scholarships, Community Service Providers, Goods, Operating Costs expenditure from this line items.

55. As required by disbursement letter of the World Bank, Department of Education has to submit details of activities under Civil works, Procurement of Goods, Consultant's Services, Community Service Providers, Training, Grants and Scholarships. To collect such information from all the cost centres takes considerably a long time and disbursement remains pending until then. Similarly, all the taxes are ineligible items for reimbursement. Recalculation of tax items from each payment and deducting same from basket and charging it to HMG's source is an arduous task for the Department.

D. Implications

56. 1. CIP main basket, non-core other development programmes and non-core development programme budget are mixed together while reaching at district. Under such circumstance monitoring of financial status and physical progress by type of programme as stated above would be quite cumbersome. It would require a tremendous time and efforts to scrutinise the type of expenditure only corresponding to basket funding. It would cause delays in reimbursement claim and on preparing the project financial statement (Project Accounts).

2. Project personnel have the opinion that the requirement of submission of details of payment with SOEs results delay in processing the expenditure under different categories, delays in charging of expenditure in special account, delays to submit withdrawal application and delays in submitting Project Account.

D. Action Taken for Improvement

57. From fiscal year 2001/2002, budget subhead 65-4-411 and 65-5-411 is used only for CIP and UNICEF budget. Similarly, no allocation of budget is made this year at Central level for district programme. In addition, SOE format is simplified to make the withdrawal application as easy as possible. All the cost centres are directed to maintain a separate ledger to enable them to submit component and category wise expenditure reports on monthly basis that meets the requirement of WB.

E. Further Actions Required for Improvement

58. Following actions are suggested to improve the funds flow and reporting mechanism of basket funding in BPEP II:

1. The definition of cost components like grants and scholarships are to be defined clearly.
2. The government should improve the line item code to add the code as per the requirements of line ministries. Scholarships and Programme Operating Costs like TADA for programme operation, NGOs Costs, Community Service Providers Costs, Procurement and Production costs are not clearly segregated for accounting purpose in separate headings.
3. DOE should give clear directives to all the cost centres on implementation procedure for each component and categories to standardise the accounting ensure the uniformity at all the cost centres.
4. Intensive training based on basket funding should be given to all the accounting staff.
5. Mixing of all CIP, Non CIP and Non CIP HMG regular budgets at district level asking the junior level account staff to keep donor wise, program wise and component wise as well as the physical, financial and category wise report made the financial management system more complicated. The present initiatives of differentiating CIP and non-CIP funding may help to simplify the procedures to some extent.
6. Tax problems can be solved by increasing the proportionate share of the government with the consent of funding agencies and approval from ministry of finance so that the expending unit and PIU need not to recalculate the tax on each payment.
7. Roles and responsibilities of each and every stakeholder should be defined at the time of agreement.
8. A discrete modality to release the budget may be agreed with FCGO and subsequent release of funds including reimbursable may be arranged through DTCOs in an efficient way by adopting HMG/N normal accounting and budgetary practices.

F. A Third Party Review

59. A third party has assessed the budgetary Performance of BPEP including other things in March 2002. Following observations were made by the assessment in financial administration

1. In those two years budget release was made at a snail's pace leading to a low budgetary performance.
2. There were difficulties in planning and budgeting of civil works, especially in the specification of the use of locally unavailable materials were incorporated.
3. The programming and costing of locally unavailable items were also less rigorous because of lack of capacity at the district level.
4. Regarding the procurement of goods and services, the familiarity with the agreed IDA's Loan Administration Change Initiative norms/standards was difficult to meet.
5. Although the training were provided to the financial officers it was of a general nature and it failed to orient them well to the LACI to the desired extent.
6. As per the report problem still abounds in financial reporting because of imperfect financial statements, including that of the basket funding and this has caused a delay in reimbursement. It was reported that inconsistent financial reporting arose due to lack of adequate familiarity with the IDA norms/LACI and the guidelines on expenditure categorisation as per the Loan Administration Change Initiatives which was developed late.

7. The other problem the Department faced was due to large number of cost centres.

Workings staff are widely vary in competency and capabilities.

8. The BPEP - II as a program, incorporates a large number of activities, including 17 components in the CIP. Consequently it is always not easy to manage in terms of accounting and reporting by each district.

Actual flow of funds and accounts with time frame in BPEP II Basket fund for the F/Y 2000/2001 is attached. Improved flow of fund with identified problem areas in a chart is also annexed

60. In conclusion, frequent change in leadership; time taken to operationalize the program together with the staff orientation; shift from project approach to program approach demanded significant procedural changes in a new context of decentralised planning, programming, budgeting and implementation and insufficient training all together helped to aggravate the problem.

61. Basket mechanism is principally adopted to minimise the accounting and operational procedures for smooth flow of funds to the beneficiaries. It is quite obvious that accounting is minimised at district level. About funds flow it is still not sure whether the system has contributed significantly to improve it.

62. There is scope for improvement in the system. Improve financial monitoring and reporting; link financial reporting with physical reporting; discourage budgetary allocations at central level for district level programme; retain trained staff and leadership for a reasonable time period; orient staff to manage basket funding; make expenditure headings compatible to the activities and clear understanding between the donors and HMG are essential for the efficient and effective implementation of the project.

VII. FINDINGS AND RECOMMENDATION

A. Findings

63. The study team has undergone a quick review of lists of documents including Acts, Regulation, study reports and has discussed with a few concerned. Followings are the findings of the study:

(1) The demand of secondary education is going to increase due to increased access and retention in primary education to achieve the education for all by 2015.

(2) With the increased number of schools and students the access of women, poor and disadvantaged on quality education has to be ensured.

(3) HMG/N with the support of Danida and ADB, is planning to implement Secondary Education Development Project in 10 districts on pilot basis from January 2003 to December 2007.

(4) A basket funding modality (putting all the donors fund in a basket, keeping integrated accounts at district and following unified procurement guidelines) was introduced in BPEP II some three year back. The project has faced a lot of challenges while adopting the system. Now the situation is quite improved particularly, in financial management.

(5) HMG/N, Danida and ADB agreed in principle to adopt the basket funding modality to simplify the procedures but the funding agencies were desirous to ensure the compatibility of procurement/funding modalities and smooth flow of fund to the beneficiaries in time.

(6) The Department of Education has been facing problems on basket fundings due to, among other were unskilled accountant at districts; problem of timely publication of source book; complexities due to details of expenses required for withdrawal from World Bank; complexities due to numerous CIP and non CIP activities to be captured in component wise progress report and difficulty to segregate expenses due to incompatibility of HMG/N line item with project categories. HMG/N has recently revised the line items of the expenditures in compliance with the GFS issued by International Monetary fund. Now line items for programme TADA and Scholarship are specified

(7) Basically following four funding models were observed in previous studies but further clarities were deemed necessary.

- Extend BPEP II basket model to secondary education
- Establish separate basket for BPEP II
- Parallel funding by individual donors as they fund for other projects
- A hybrid of two or more

(8) In addition to this recent movement in decentralization, 7th amendment in Education Act, 10th Five Year Plan, MTEF and PERC report have proposed / perceived the education service delivery in their own perspective. A very recent move (a meeting with the line agency officials and MOLD on third week of April, 2002) is indicative that the agencies may agree to devolve the some of the services at district level including basic and primary education.

(9) Prior approval of HMG/N is required for direct funding to DDC from foreign sources.

(10) If the number of funding agencies in SESP is limited to two/three the parallel system could also be adopted but the project has envisaged to invite other donors as well. If there are many donors to finance the project individually with a parallel funding system than the executing units have to keep separate bank accounts, separate sets of books, submit separate reporting formats and follow different procurement procedures. The whole system may be too cumbersome and complex to adopt at district.

(11) Training on accounting from BPEP II to district level staff was too general which could not fulfil the specific needs of the financial management of the program.

(12) To introduce a hybrid system of BPEP and others number of activities intensive preparation, training, designing manuals and guidelines etc. are required.

(13) World Bank and ADB have extensive guidelines for funding, disbursement and procurements. The WB guidelines of procurement and disbursement are followed in BPEP II.

(14) All the funding agencies have the intension/objective to strengthen the government system rather than creating a parallel one.

(15) Funding agencies are desirous to ensure an accounting system which records quantitative and financial data; a reporting system which includes quantitative and qualitative results and financial data and a funds flow system that ensures the smooth execution. HMG/N's rules,

regulation, relating to provision on financial transaction, reporting and procurements are almost compatible to international standard and are comprehensive. The major problem is competency of the staff involved and compliance. There is also a short fall of a document to depict the activity wise accounting along with financial reports.

(16)Funding agencies are desirous to have a strong local self-government.

(17)Auditing of small amount at grass root level is a costly business. Sample and test check can be introduced relying standard reporting from the rest of the units.

(18)The government is desirous to have all the funds from donors (including TA fund) be reflected in Government Budget.

(19) The different funding proportions of HMG/N and donor in different categories create complications in keeping account and getting reimbursements. Calculation of taxes from each bill at local level offices to obtain the actual reimbursable amount is too complex which has hampered the timely replenishment of fund.

(20)Internal control, roles and responsibilities of centre, district, village and grass root level organizations are not well defined.

B. Recommendation

64. Based on the analysis done, documents reviewed, personnel met in the relevant field and our best judgement and understanding, the study team would like to recommend the followings:

(1) ADB's procurement, accounting, auditing and reporting systems/procedures are of international standard and can be relied upon by the bi-lateral agencies.

(2) Internal control, checks and balances in an ADB funded project are sufficiently devised. The system can be used as a common funding modality in SESP.

(3) The government's reform process in the field of decentralization has not yet taken its distinct shape. Present acts and regulations also do not prohibit funding LGIs by taking prior approval of the government. However, it is not recommended to fund LGIs directly by project loans and program grants together in a basket. But DDC can be an implementing agency for both the funds keeping together in a basket.

(4) A parallel funding modality would not meet the objective of "promoting coherence on the part of donor involvement in SESP and possible involvement of other donors in future". This modality also requires extensive clerical work at field level. Therefore, we would not like to suggest following parallel model.

- (5) A hybrid approach would demand a considerable exercise and rigorous training to the staff and should start from scratch. It is quite obvious that internal control would be much more complex in a situation operating various modalities at a time. Therefore the hybrid model is not desirable for the program under consideration. However, whichever model we follow an extensive training to the finance staff could improve the funds flow and reporting. Therefore it is strongly recommended to conduct such training before/during the programme.**
- (6) In a context of HMG/N and funding agencies working closely to harmonise funding modalities, a similar system as adopted in BPEP II is recommended to replicate in SESP as well with few modification as suggested in a flow chart.**
- (7) Danida direct funding up to the agreed percentage can be used as the development**
finance directly to District Development Committees and technical support at central level as well.

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Annex I

Direct Funding Mechanism of Danida

Step 1.
Agreement between HMG Royal Danish Government

Step 2.
Project Support Office (PSO) of Danida requests the fund through local Danish Embassy.

Step 3.
The embassy releases the fund to the PSO account

Step 4.
Determined activities are carried on either an agreement with spending units or make direct payment to the activity specified in the project or programme. Approval of line ministry is sought if deemed necessary.

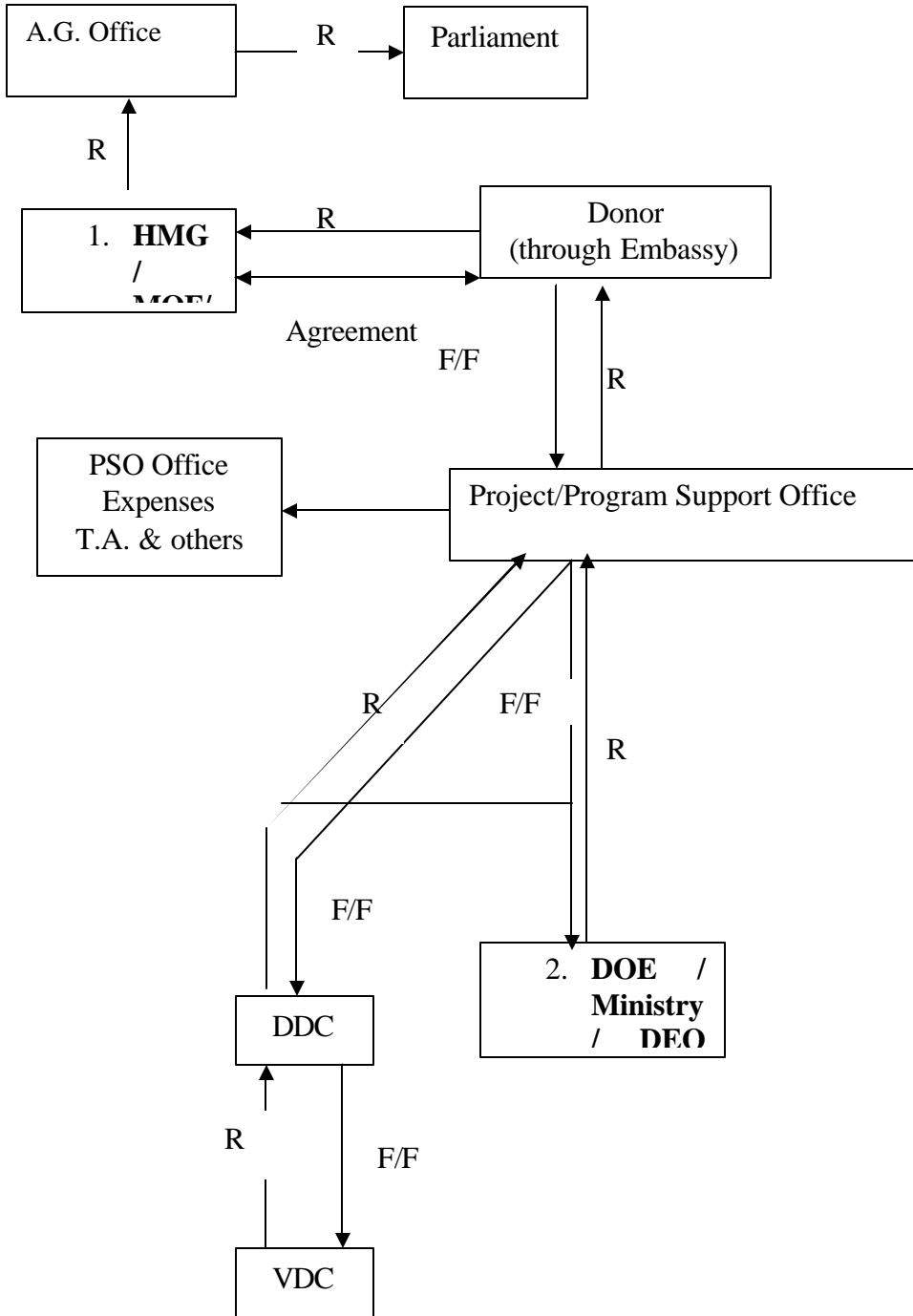
Step 5.
Monitoring is done sometime directly and sometime through Departments/DDCs.

Step 6.
Reporting is required as per the agreement with spending unit. Spending unit reports either directly to PSO or DDC/Department. PSO has to report Danish embassy. Danish embassy reports to Danish Government and HMG/N. Similarly HMG/N reports to AGO and Parliament.

Step 7.
Local Auditor is also appointed by Danish embassy. Auditing of the accounts come under the jurisdiction of Auditor General of Denmark. Local Auditor required to report six monthly. Accountability lies on PSO and Danish embassy,

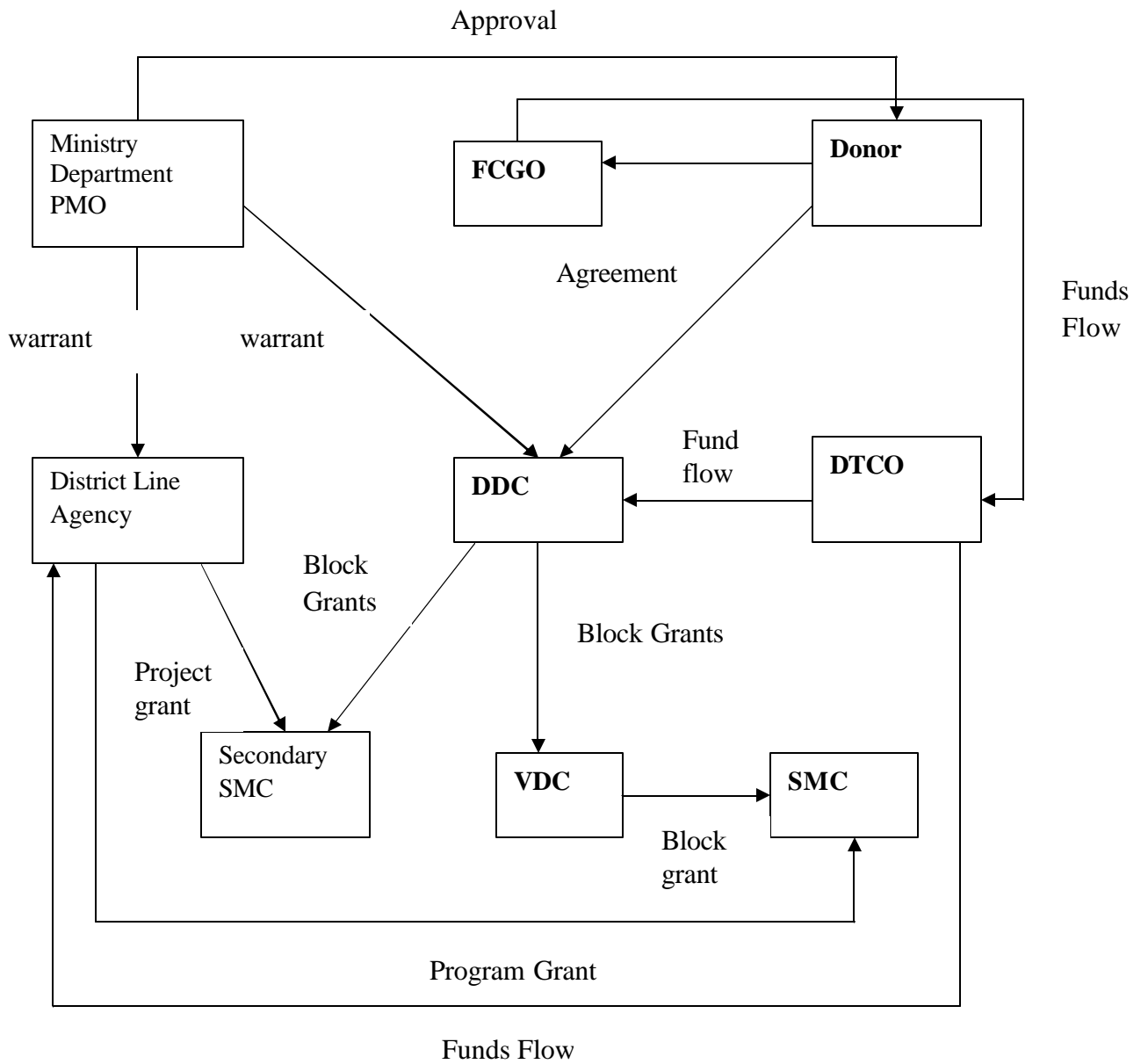
1.2. Annex II

Direct Funding



Note:
 F/F = Fund Flow
 R = Reporting
 Accountability = P.S. office
 & Donor

Annex III
Fund Flow
 (centralize System)



Annex IV
Flow of Activities in District Development Fund (DDF)

1. Ensure the Availability of Fund, Priority, Guidelines from Center and Feasibility of the project under consideration
2. Plan Program and Budget Approved by District Council
3. Work Plan Prepared by District Council
4. Monitoring and Supervision team constituted
5. Project implemented expenses incurred are paid from DDF. The fund is operated with the signature of Secretary and financial administration chief, expenses are approved by chair person/secretary as per the limit of regulation
6. Internal auditing is done by DDC and external by AGO or designated
7. Reporting to DDC and ultimately to DC which, sits twice a year normally
8. Audit committee formed with a chair of one of the DDC members and report of audit committee as well as auditor are presented to District Council
9. Co-ordination is required with the sectoral offices to check the duplication

Annex V

A comparative Chart of Variances in NCB Procurement guidelines in between HMG/N, IDA, Danida and ADB

Provisions required under IDA Procurement Guidelines	Provisions required under ADB Procurement Guidelines	Provisions under Financial Rules and Regulation in Nepal	
1. Advertisement in a national newspaper of wide circulation	Advertisement in a national newspaper of wide circulation	Based on the estimated value of the contract, bids may be advertised at district level in a local newspaper (<10 lakhs)	3m E above adver
2. Sealed quotation procedure is treated as tender and should follow NCB procedure	Sealed quotation procedure is not in practice	Separate procedure	Direc from certai is all
3. At least 30 days preparation time	At least 30 days preparation time	Depending upon the estimated value of the Contracts the bidding period varies from 15 to 90days. The rules also permits 10 days notice for the procurement costing less than 10 lakhs. (sealed quotation)	Not s
4. Bid documents made available even by mail if so requested	Not mailed	Not mailed	By le 3m E
5. Evaluation done in accordance with criteria that are determined in advance in the bid documents	Evaluation done in accordance with criteria that are determined in advance in the bid documents	Evaluation done in accordance with criteria that are determined in advance in the bid documents but generally not complied	Evalu criter menti guide
6. Evaluation done in standard formats	Evaluation done in standard formats	The standard formats are not prescribed	Evalu done form:
7. Bid opened in one place in public immediately after the deadline for submission	Bid opened in one place in public immediately after the deadline for submission	a. Public opening is mandatory b. Bids are normally not opened immediately after deadline for submission but opening date is published in advance.	Open tende take j colle the e limit
not allowed	not allowed	c. The rule allows for bids to be received and opened at more than one place	not sj
8. No preference to national bidders in NCB 7.5% in ICB	No preference to national bidders	National bidders and their ventures are awarded preference 10p.c.	Prefe Donc
9. Award must go to lowest evaluated Bidder	Award must go to substantially lowest evaluated bidder	Award must go to substantially lowest evaluated bidder	Awar to the who's finan favou and c
10. Negotiations not permitted with lowest evaluated	Negotiations permitted with lowest evaluated Bidder or any	Not permitted	Nego equal

Bidder or any other Bidder	other Bidder		to all
11. Direct contracting at nationally negotiated rates not accepted	Direct contracting at nationally negotiated rates not accepted	Rules permit direct contracting	Direct contracting permitted
12. Bid validity period 90 days plus at least 28 days	Bid validity period 90 days plus at least 28 days	Not mentioned	Not mentioned
13. Standard formats prescribed for Bid Bond and performance Bond	Standard formats prescribed for Bid Bond and performance Bond	Not prescribed	Not prescribed
14. Cost of the bid document is not mentioned but should not be more than the actual cost it takes for bid preparation	Not mentioned but it is mentioned that cost should not be more than the actual cost it takes for bid preparation	The cost of Bid Document varies from NRs. 1500 to 4000	Not mentioned
15. Do not allow to reject the bid if there is only one responsive evaluated bid	Do not allow to reject the bid if there is only one responsive evaluated bid	Should reject the bid if there is only one responsive evaluated bid unless it is justified.	Not specified

Annex VI

Comparative Charts of Financial Managements Practices and Requirement of HMG/World Bank/ADB/DANIDA

Item	HMG	World Bank	ADB	
General	Comprehensive financial rules & regulations; cash base accounting; Donor's fund required to incorporate in National Budget; separate enactment & rules for decentralization practices & procedures; provision for independent auditor	Extensive framework for financial monitoring & auditing; financial accountability assessment is done both for country & project specific; reporting & auditing requirements are based on the assessment of level of risk & complexity of the project; International auditing guidelines are followed; bank may inspect or review bank financed project accounts and audit reports	Extensive framework for loan disbursement & reporting; international accounting & auditing guidelines are followed; specific recording & reporting are as per agreement; bank may inspect or review bank financed project/reports	No specific accounting system. But reporting satisfactory by auditor. Competitor by auditor expenditure linked into performance the principle external & appropriate likes to in management responsible accounting auditing operation
Planning	Central/Local level	As agreed	As agreed	As agreed

Budgeting	Annual approved plan Donor assistance is mandatory to be incorporate in national budget	As per borrower's annual budgeting in conformity with the agreement	As per borrower's annual budgeting in conformity with the agreement	As per bc in confor Direct fu national t reflected
Release of Fund and Disbursement	Authorised warrant is necessary for the release of fund, initial deposit of 1/6 after the approval of the budget & then reimbursement of the expenses incurred on the presentation of SOE	Advance on special AC then replenishment & reimbursement plus direct payment & commitment through authorised withdrawal application & SOE	Advance on imprest account then replenishment & reimbursement plus direct payment & commitment through authorised withdrawal application	Pre-fundi
Sealing of Initial/Imprest/Special Fund	Upto of 1/6 th of last years expenses	as per agreement	as per agreement	Pre-fundi expenditure
Accounting	Cash basis approved by HMG and subsidiary account as required by donor agreement; Individual project account & individual donor account is maintained	Cash basis or accrual as per International Accounting Standard. Financial management assessment is done before lending & additional recording & reporting arrangement is required	Cash basis or accrual as per International Accounting Standard.	Co-operat procedur
Inillegible Expenses	As agreed with the donor	Taxes & duties, cost of land acquisition or right of way; working capital other than incremental & charges other than those on bank loans & expenditure not directly connected to bank financial project.	Custom duties & other taxes on imported goods; land cost; local freight charges for imported goods; VAT; premium paid in local currencies unless provided for in the loan agreement; Interest expenditure not directly connected to bank finance project.	Not clear agreemer
Procurement	Financial rules have 40 clauses regarding procedures & process of different types of bidding. Types of bidding & ceiling are as follows: Rs.100000 –Directly from the market	Detail provision regarding process & procedures of procurement of goods, services & works; sample standard bidding document are published. Types of bidding are as follows:	Detail provision regarding process & procedures of procurement of goods, services & works & sample standard bidding document are published.	There is 1 guideline Danish ru is perspec for procu Bank's pr bidding a

	Rs.1m – Sealed quotation Rs.1m & above– tender or public bidding. On special condition direct purchase or sealed quotation of any amount with the approval of the secretary of the Ministry. domestic preference -10%	International competitive Bidding Two stage Bidding Modified International Bidding Limited International Bidding National competitive bidding Shopping (international & national) Direct contracting Force amount Procurement from UN agency Domestic preference – in ICB 7.5%	Types of bidding are as follows: International competitive Bidding Two stage Bidding International Shopping Local competitive bidding Community participation	Upto 500 50000 D letter Upto 1m 1m to 3m without a 3m & ab advertisir
Monitoring & Reporting	Periodic, normally monthly & annual reporting as per approved financial rules & accounting procedures. Additional reporting from subsidiary account as agreed with donor or as specified in Donor's Guidelines	As per specific guidelines & as agreed	As per specific guidelines & as agreed	Not speci
Auditing	Financial & Performance Auditing by Auditor General of Nepal, AGO is a constitutional body & also member of INTOSAI; there is no time frame for completion of audit but mostly in donor funded projects auditing is completed & reported as agreed or as specified in guidelines	International Auditing Standard is acceptable to World Bank. Auditing form auditor general is also accepted. Audit report is required to be submitted to the bank within 6 months after the end of fiscal year. Bank reserves the right to review the accounts & the reporting. A detail guidelines for different types of auditing & reporting is prescribed	Auditor general's auditing is acceptable to ADB. Bank requires adequate records consistently maintained in accordance with generally accepted accounting principle & audited in accordance with the auditing standard & available for review by bank. Bank may request to the recipient to prepare supplementary items of information that differ form those generally required by local auditing practices	There is 1 audited re submittec end of the
Overall Assessment	Financial rules & regulation covers every aspect of financial	System is quite impressive; focus should be given to	There is a detailed guidelines but some	No detail is follow

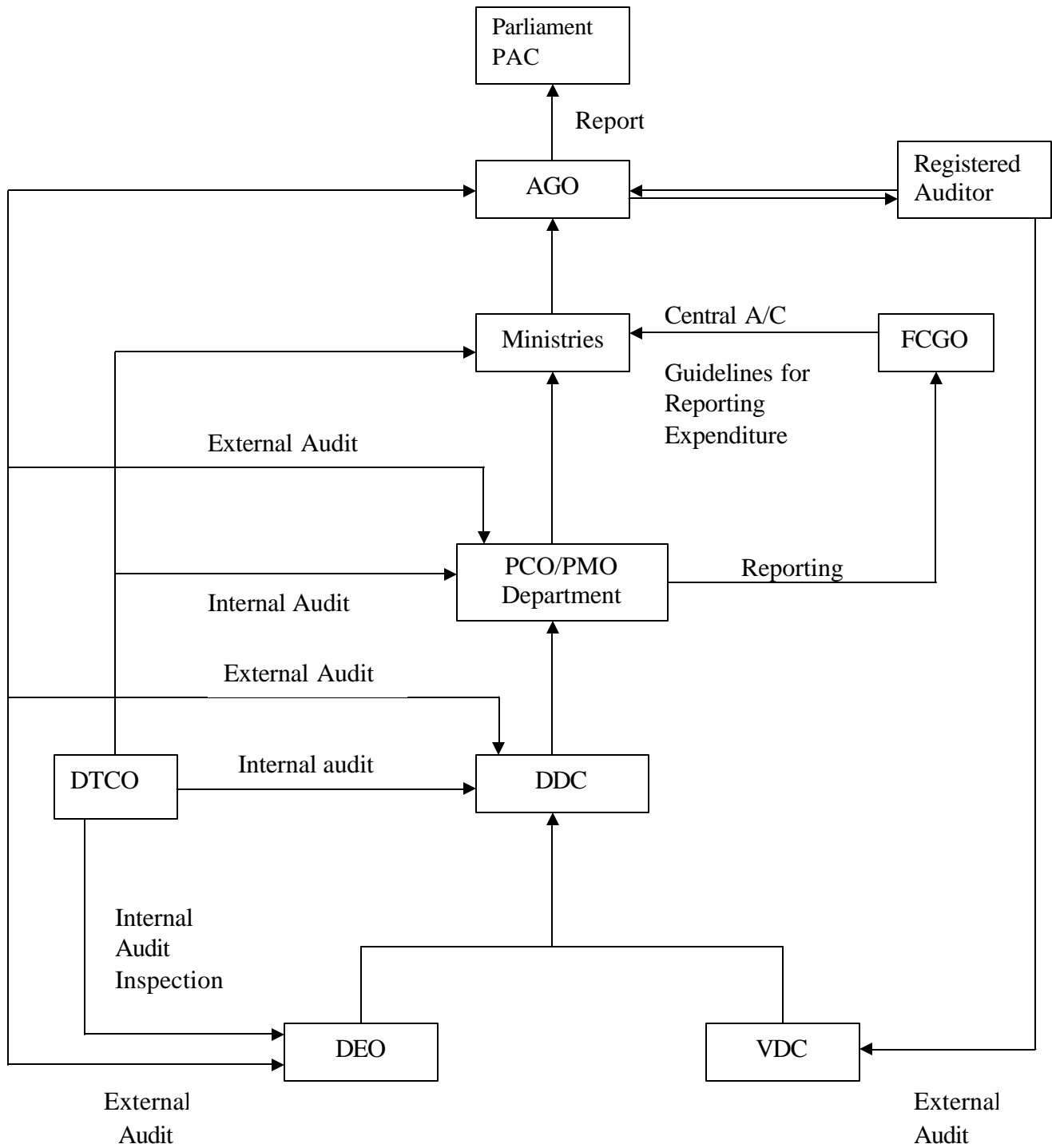
	<p>management. Accounting & auditing standards are not clearly mentioned. Compliance of the rules are not up to the satisfaction. Reporting to the donors are maintained form subsidiary accounts which is not a part of regular accounting sytem</p>	<p>strengthen national accounting & auditing system, which may differ from project to project</p>	<p>reporting formats are specific as agreed in the project agreement. Focus should be given to harmonise the system & strengthen the local capabilities</p>	<p>accountir Focus sho local syst</p>
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Annex VII

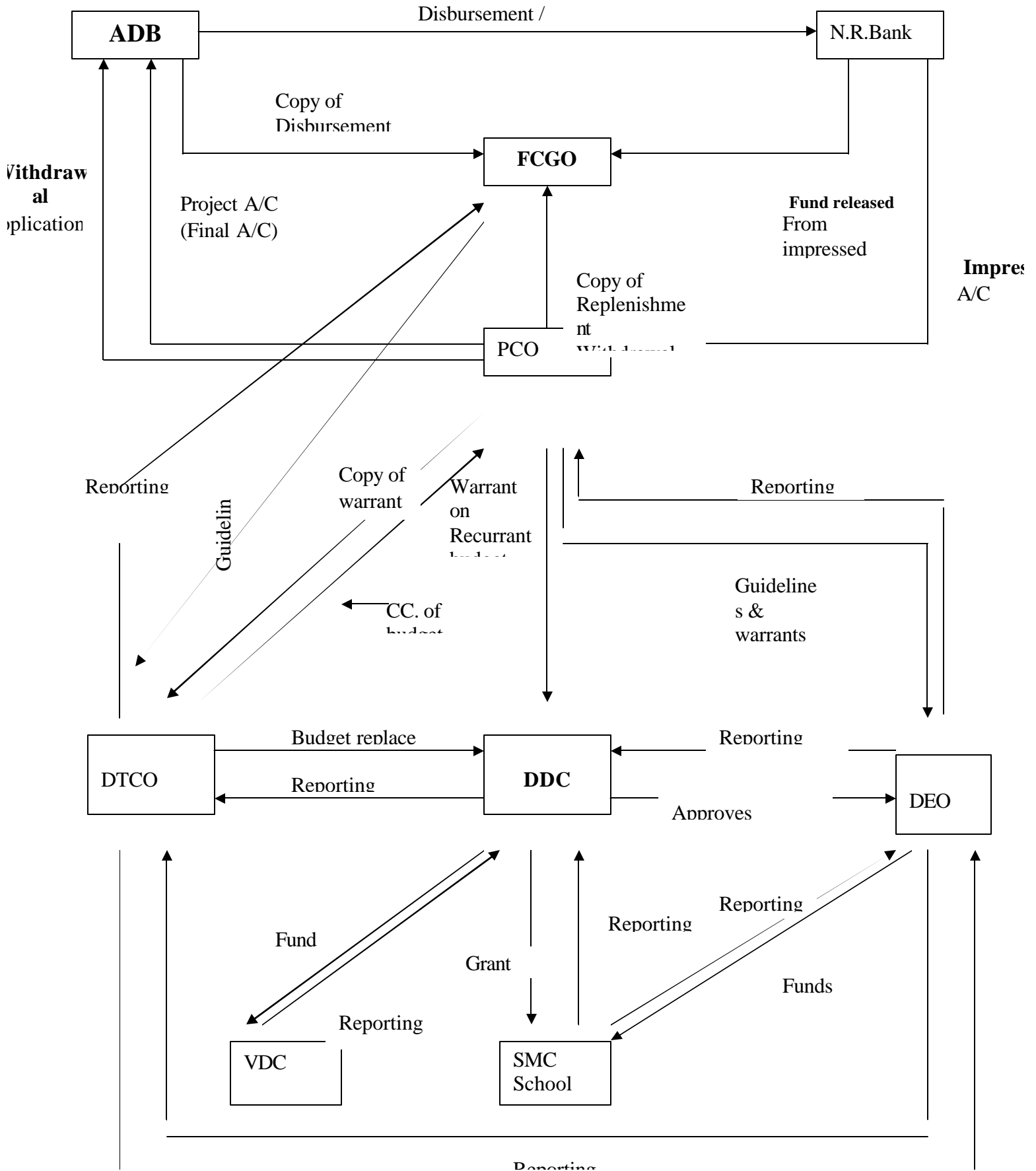
Comparative Assessment of Auditing Accounting and Reporting System

	HMG	IDA	ADB	DANIDA
1. Accounting System	Double Entry and Cash Basis	Accepted	Accepted	Accepted
2. Reporting Financial	HMG Expenditure Code	Disbursement Code (Category)	Disbursement Code (Category)	Not specific but should be linked into sector progress indicator
3. Disbursement	Monthly Expenditure Statement (AGF 13,14,15) Regulation Annex 2	SOE/Details of Payments	SOE/Details of Payments	Sufficient documentation or Government's SOE accepted
4. Financial Statement	AGF 17	Project management Report	Project management Report	Project management Report
5. Time for Certificate	not clear	6 months	6 months	6 months
6. Physical Progress	Standard Format Annex II of financial rules	Standard Format under PMR-based Disbursement Now FMR based	As dictated under the project Administrative Memorandum (PAM)	Not Specific/as agreed

Annex VIII External and Internal Control

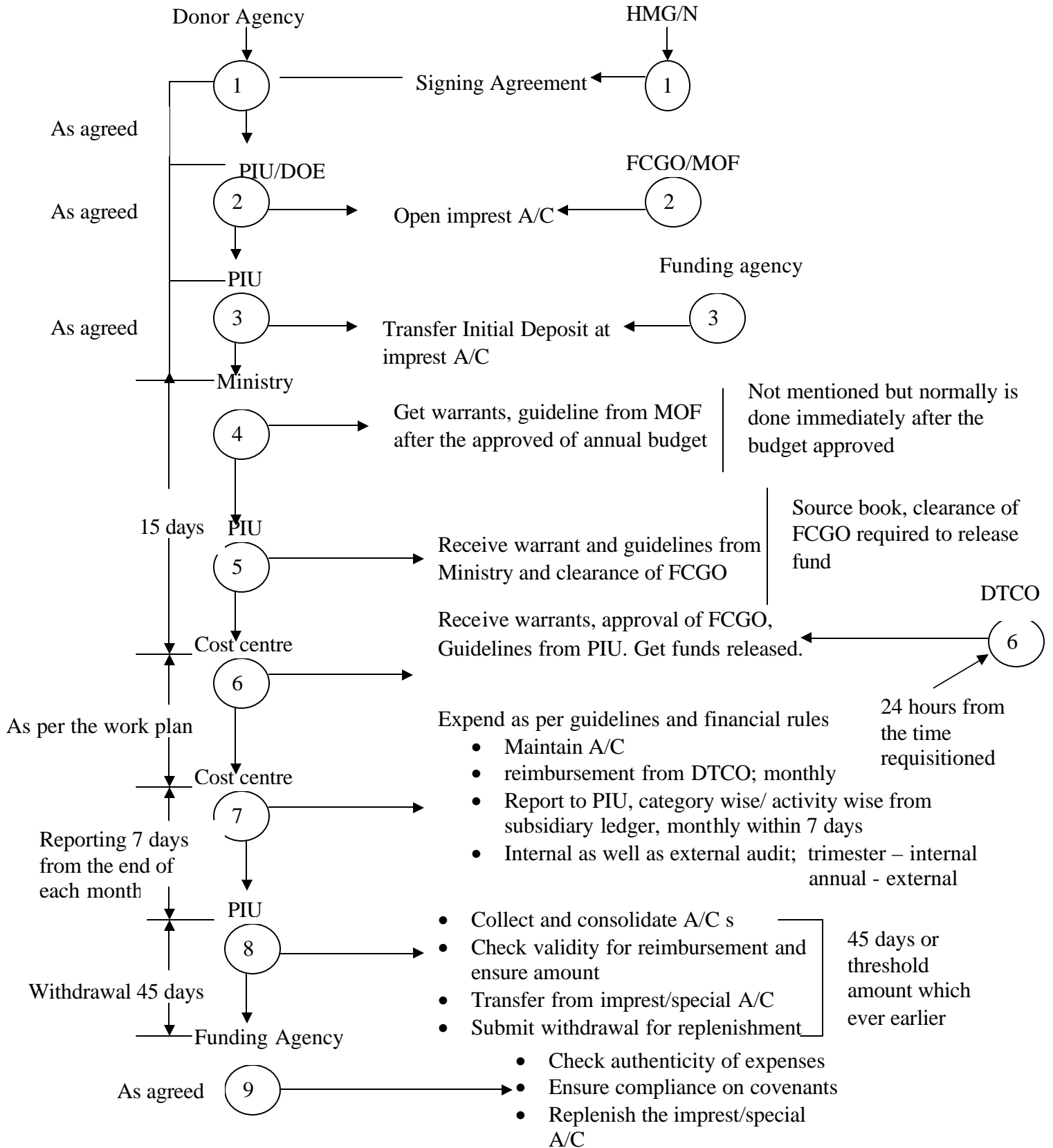


Annex IX
Funds Flow and Reporting
ADB – HMG/N



Monitoring

Annex X
Funds Flow / Flow Chart
Loan A/C / Donor's A/C



Annex XI
Actual Flow chart of Funds and Accounts of Basket Fund (F.Y. 2000/01)

- 1 Fiscal Year started 16th July, 2000
- 2 Warrant issued from Ministry of Finance to MOES 25th July, 2000
- 3 MOES issued Warrant to the Department of Education 27th July, 2000
- 4 Department issued Warrants to Offices 8th August, 2000
- 5 FCGO – Recommended for Fund release – Ist trimaster 1st November, 2000
- 6 FCGO – Recommended for Fund release – II nd trimaster 30th November, 2000
- 7 FCGO – Recommended for first Fund release – III rd trimaster 27th April, 2001
- 8 Integrated Financial Report Prepared 22nd March, 2002
- 9 Unaudited Project Account attested from FCGO 1st April, 2002
- 10 Unaudited Project Account sent to WB 4th April. 2002
- 11 Audited Project Account sent to WB 14th April. 2002

Note (Source DOE): (1) First Quarter Starts on -----16th July
 Ends on -----15th November

(2) Second Quarter | Starts on-----16th November
 | Ends on -----15th March

(3) Third Quarter | Starts on----- 16th March
 | Ends on ----- 15th July

Annex XII
Flow of Fund (Basket Fund)
<Improved>

What	Who	When
1. Put money on basket	Funding Agency – Ministry of Education, MOF	First week of Shrawan
2. Determine the funding modality + shares	Funding Agency – Ministry of Education, MOF	First week of Shrawan
3. Issue one warrant as HMG Development Budget	MOF, MOES and DOE	15 days
4. Expend, Monitor and A/C at district level	DDC, DEO	As per AWP, Regular
5. Reporting	DEO	7 day of the end of month
6. Consolidate accounts, ensure compliance of guidelines	DOE	45 days
7. Withdrawal Application	DOE	Within 52 days of the end of month
8. Disbursement / Replenishment	Funding Agency	Put time frame
9. Review	HMG and Funding Agency	Every 4 month

Present Process of Basket Funding

Step One

Put money in imprest account

Step Two

Approve budget and issue warrants (authority to expend)

Step Three

Receive Source book from MoF and clearance from FCGO for Budget Release

Step Four

Disbursement of Budget from DTCO

Step Five

Expenses incurred and Account Maintained

Step Six

Reporting to DoE

Step Seven

Consolidation and verification of expenditures at DoE

Step Eight

Transfer funds from Imprest/ special a/c to treasury

Step Nine

Withdrawal application and Replenishment from funding agency

Problem Areas 1: Step three due to Source book	Solution: Release Budget form Single Source HMG/Development but Approval from MoF
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	required
Problem Areas 2: Step Five due to recording transactions activity and source wise	Solution: As the fund is kept in Basket no source wise record is required
Problem Areas 3: Record transaction and reporting	Solution: Intensive training to field level staff and retention up to reasonable period
Problem Areas 4: Step seven and Nine due to details of activities	Solution: Funding agencies can rely on the internal control mechanism or introduce such a mechanism so that each and every detail of bills is not required. Sample checking in detail is also suggested.
Procurement related problem due to inability to fulfill the standard of procurement including standard specification of materials	Solution: Review the standards and specification of materials/procurement at district level

Annex XIII
List of documents and books reviewed

S. No.	1.3. Name of the documents
1.	Asian Development Bank Financial Reporting and Auditing of Projects Financed by the bank
2.	Audit Report of BPEP II; 14 May, 2001
3	Basic and Primary Education Programme Manual on Financial Management Accounting System Presented by Chandra Bdr. Shrestha
4.	Budget 2058/59
5.	Budget formulation Manual 2057
6.	DAC TASK FORCE ON DONOR PRACTICES financial Reporting & Auditing Draft Report 18 March, 2002 By Torun Reite & Jens Clausen
7.	DANIDA Guidelines for Sector Programme Support
8.	Decentralised Project Accounting April 1996 (Danida)
9.	Disbursement Handbook W/B
10..	Draft Education Regulation 2058 HMG/N
11.	Economic Survey 2057/58 HMG/N
12.	Education (DANIDA SECTOR POLICIES)
13	Education Act in Nepali HMG/N
14.	Evaluation Guidelines February 1999
15.	Financial Accounting Reporting & Auditing Handbook W/B
16.	Financial Administrative Regulation 2056 English, HMG/N
17.	Framework for Accounting (BPEP II)
18.	Financial Management Procedure – Mr. Nemkul (BPEP II)
19.	Financial Monitoring Reports: Guidelines to Staff November 30, Danida
20.	Financial Training Manual Nepali & English BPEP II
21.	Guidelines for Procurement under Asian Development Bank Loans
22.	Guidelines for Support to Financial Services (Danida)
23.	General Guidelines (Danida)
24.	Guidelines on the use of consultants by Asian Development and Its Borrowers (ADB)
25	Guidelines Procurement under IBRD Loans and IDA Credits
26	Guidelines Selection and Employment of consultants by World Bank Borrowers (Revised January 1999)
27	Loan Disbursement Handbook June ADB
28	Local Authorities Fiscal Commission Report, 2002 HMG/N
29	Local Governance Strengthening Programme HMG/N
30.	Medium Term Expenditure Framework HMG/N
31.	PIP (BPEP II)
32.	Preparation for future Danish Support to secondary Education in Nepal
33.	Rules and Guidelines for the Procurement of Goods September 1994 Danida
34.	Resource forecast and budget preparation guidelines HMG/N
35.	Technical Panel Report BPEP II

36.	Warrant and budget execution guidelines (MOF)
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Annex XIV
List of persons visited / consulted

Mr. Bal Bahadur K.C.	DEO
Mr. Bandhu Rajan	DASU
Mr. Fanidra Regmi	MOES
Mr. Dilip Raj Joshi	DOE
Mr. Ganga Datta Awasti	MOLD
Mr. Hikmatman Bista	DASU
Mr. Krishna Ram Pandey	ADB
Mr. Shakti Prasad Shrestha	FCGO
Mr. Vigyan Pradhan	WB
Mr. Rameshore Khanal	FCGO

Annex XV
List of Abbreviations:

ADB	- Asian Development Bank
AGO	- Auditor Generals Office
BPEP	- Basic and Primary Education Program
CBOs	- Community Based Organisation
CIP	- Core Investment Plan
DASU	- Decentralization Advisory Support Units
DDC	- District Development Committee
DEC/VEC	- District Education Committee/ Village Education Committee
DEO	- District Education Office
DOE	- Department of Education
DTCO	- District Treasury Comptroller Office
EC	- European Commission
FCGO	- Financial Comptroller General Office
HMG/N	- His Majesty's Government of Nepal
ICB	- International Competitive Bidding
IDA	- International Development Association
INTOSAI	- International Organisation of Supreme Audit Institution
JICA	- Japan International Cooperation Agency
LACI	- Loan Administration Change Initiative
LGI	- Local Government Institution
LGSP	- Local Government Strengthening Program
LSGA	- Local-Self Governance Act
MOES	- Ministry of Education and Sports
MTEF	- Medium Term Education Framework
NCB	- National Competitive Bidding
NCTD	- National Council for Training and Development
NGO	- Non Government Organisation
NPC	- National Planning Commission
PAT	- Programme Advisory Team
PIU	- Project Implementation Unit
PSO	- Project / Programme Support Office
RED	- Regional Education Directorate
SEDP	- Secondary Education Development Plan
SEDU	- Secondary Education Development Unit
SESP	- Secondary Education Support Program
SMC	- School Management Committee
SOE	- Statement of Expenditure
UNICEF	- United National Children's Fund
VC	- Village Committee
VDC	- Village Development Committee
WB	- World Bank

Annex XVI

TOR

The draft Core Document for SEPS assumes a basket approach to funding in line with that adopted in BPEP II. While this approach is the most favourable for the sector programme approach, a number of factors need to be addressed by the Appraisal Mission:

- (i) Adopting a basket approach is expected to require that ADB financial procedures for loan funds to a 'project' be followed. It is important that the full implications of this arrangement be appraised prior to finalising the programme documentation. In particular, the consequence of adopting procurement rules, component and sub-component budgeting, auditing and other requirements, need to be assessed.
- (ii) The SESP documentation indicates two possibilities for Danida direct funding. In one, Danida direct funding will be primarily limited to support for technical assistance. In the second scenario, Danida direct funding will also include funding for implementation of the intensive strategy in 10 districts. The mission needs to appraise whether or not the government reform process in the field of decentralisation clearly and irrefutably supports the financial decentralisation that would permit and support such use of direct funding. When this is clarified, the proportion of direct to basket funds provided by Danida can be more firmly established.
- (iii) The relation between the donor funding to SESP and the national budget needs to be made clear during the appraisal mission. This means integration into the HMG system, and utilisation of appropriate HMG channels. At the same time, it must be ensured that funds will reach the beneficiaries – including the communities and the schools at the initiation of the Nepalese fiscal year. The appraisal will confirm the fund flow and reporting/audit requirements.
- (iv) In order to promote coherence on the part of donor involvement in the education sector, the financial requirements, rules and regulations of HMG, ADB, World Bank and Danida need to be compared so that the financial administration of BPEP II and SESP can be as similar as possible. This should be appraised on the management requirements (this work can be done as desk work in Nepal in advance of the mission).

Annex XVII
WORK ACTIVITY AND IMPLEMENTATION SCHEDULE

S.No	Activities	Duration	Date
1.	Collection of Documents And Review	5 days	May 20 th , Monday May 21 st , Tuesday May 22 nd , Wednesday May 23 rd , Thursday And May 24 th , Friday
2.	Preparation of Preliminary Draft Report	3 days	May 25 th , Saturday May 27 th , Monday And May 28 th , Tuesday
3.	Interaction with World Bank, ADB, DANIDA and HMG	1 day	May 29 th , Wednesday
4.	Adjustment of Suggestions	1 day	May 30 th , Thursday
5.	Discussion with Financial Management Consultant	1 day	May 31 st , Friday
6.	Preparation of Draft Report	3 days	June 1 st , Saturday June 2 nd , Sunday And June 3 rd , Monday
7.	Preparation of Draft Final Report and Review by Financial Management Consultant and PAT Office	1 day	June 4 th , Tuesday
8.	Adjustment and incorporation of suggestions in Final report	1 day	June 5 th , Wednesday
9.	Presentation of Final Report	1 day	June 6 th , Thursday

