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On the
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AID FINANCING AND AID EFFECTIVENESS

Attached for the September 25, 2005, Development Committee Meeting is a progress report entitled "Aid Financing and Aid Effectiveness," prepared by the staff of the World Bank with contributions from the staff of the International Monetary Fund.

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September 13, 2005

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I. INTRODUCTION

1. Progress in recent years on the aid effectiveness agenda has considerably reduced the tension between the call for adequate and predictable commitment of resources, and concern about the effective use of available resources. Enhanced policies and institutional frameworks in developing countries, improved performance-based allocation mechanisms, strengthened results-oriented frameworks, and increased harmonization and alignment have all contributed to this development.

2. In response, a range of important additional financing commitments have been announced over the past six months, including at the G8 Gleneagles Summit, which set a broad development agenda focused on Africa, with additional financial commitments and debt relief matched by steps to improve development effectiveness.

3. To help ensure full implementation and effective utilization of these unprecedented commitments, including the doubling of aid to Africa, the G8 called on the World Bank to take a leading role in helping to ensure that additional assistance is effectively coordinated and in supporting the partnership among the G8, other donors, and recipient countries, including in Africa. By its nature, this role will require very close partnership with the Development Assistance Committee of the OECD (OECD-DAC), the United Nations Development Group (UNDG), the IMF and other Multilateral Development Banks.

4. Against this background, the present note responds to the requests made by the Development Committee at the 2005 Spring Meetings:

- The Development Committee "welcomed the Paris Declaration on Aid Effectiveness, … urged the establishment of targets, as agreed, for each of the indicators for 2010" and "called on the Bank to show leadership by example, in implementing the Paris framework."
- The Development Committee also "confirmed [the] commitment to deliver on the pledges made at and after Monterrey to raise levels of ODA," "welcomed further work on innovative sources of development financing," "encourage(d) interested donors to proceed with [the] proposals" and, "building upon the existing political momentum in some countries, … invite[d] the Bank and the Fund to deepen their analysis of the most promising nationally applied and internationally coordinated taxes for development for the Annual Meetings, as an input into the consideration of a pilot case for interested countries."

5. The purpose of this note is three-fold:

- First, it takes stock of new aid commitments and proposes an enhanced framework for monitoring, reporting and follow-up on the delivery of aid commitments;
- Second, it reports on progress to date on financing modalities, including innovative financing mechanisms, that can help support increases in aid commitments but without undermining the coherence of the aid architecture;
- Third, it reports on progress to date on the aid effectiveness agenda, including the Managing for Results agenda and on alignment and harmonization.

II. ENSURING DELIVERY ON AID COMMITMENTS

6. As a result of successive announcements of higher aid commitments since Monterrey, including major increases announced over the past year, there is a prospect of a very substantial increase in official development assistance over the coming five years. In April 2005, the DAC/OECD estimated that on the basis of commitments made by DAC members, total ODA could increase by $36 billion in real terms by 2010 from the 2004 level. Since then, the European Union (EU) has announced sharply higher targets for 2010 than for 2006 and Japan announced a $10 billion increase in its aggregate ODA over the next five years. Based on the new announcements, total ODA is now projected to increase by around $50 billion in real terms by 2010. Over 70% of the increase would come from EU donors. Announcements over the past year imply a substantial improvement from low levels reached in 2001, but still leave DAC donor countries as a group well short of the UN target (0.7% of GNI). Five of the 22 DAC member countries (Denmark, Luxemburg, Netherlands, Norway, and Sweden) have already raised ODA to over 0.7% of their GNI; Five additional countries (Belgium, Finland, France, Spain, and UK) and the EU as whole have set an explicit timetable for raising ODA/GNI to the 0.7% level[1].

7. The G8 has also made a specific commitment to double aid to sub-Saharan Africa to $50 billion in 2010. In the case of the EU, which has pledged to nearly double its ODA between 2004 and 2010, at least 50% would go to sub-Saharan Africa. The United States has also committed to double aid to sub-Saharan Africa between 2004 and 2010, and Canada between 2003/4 and 2008/9. Japan has committed to double its ODA to Africa over the next three years. Meeting the target of doubling aid to Africa would imply that half of the increase in aggregate ODA would have to be targeted for Africa (or its share in total ODA would need to rise from its current level of about 37 percent to 42 percent by 2010).

8. As highlighted in the Development Committee paper for the Spring Meetings, actual disbursements of ODA have shown a welcome reversal following nearly a decade of almost continuous decline, but have not translated into a significant increase in cash financing for the poorest countries. According to the DAC, ODA levels in nominal terms rose from $52.4 billion in 2001 to $78.6 billion in 2004[2] (0.25% of GNI compared with a low of 0.22% of GNI in 2001). The increases in real terms were more modest (around 5-6 percent per annum) because of inflation and the fall in the U.S. dollar. Moreover, much of the increase in bilateral ODA has been in the form of special purpose grants, namely for debt relief, emergency and disaster relief, technical cooperation and administrative overheads.[3] Specific donor priorities can have a major influence on the

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[1] The EU has pledged to reach 0.7 percent ODA to GNI by 2015 with a new interim collective target of 0.56 percent of ODA to GNI by 2010.

[2] 2004 data are preliminary.

[3] To the extent that debt relief lowers debt service costs, recipients gain additional fiscal space that can be used to increase spending on development programs. However the debt stock write-down component included in ODA exceeds the debt service savings by a wide margin, because many of the poorest countries were not servicing their debt in full. Although special purpose grants are essential elements of the development agenda and have budgetary consequences for donor countries, they do not provide developing countries with the additional fiscal resources required to support their poverty reduction strategies.

allocation of aid – for example, the share of ODA allocated to Afghanistan, Colombia, Iraq, Jordan and Pakistan increased from an average level of 3% over the period 1980-2000 to over 11 % in 2003. Although a detailed breakdown by component and recipient is not yet available for 2004, the amount of cash financing allocated to support PRSPs in the poorest countries is unlikely to have registered any significant increase.

9. Some important conditions will have to be met if the proposed increases in aid commitments are to be effective in supporting the scaling up of country efforts to meet the MDGs. First, commitments will have to be translated into actual delivery of aid. Second, the increases in aid will have to be targeted to the poorest countries, with at least 50% targeted to sub-Saharan Africa, and to tackling the MDG agenda in other developing countries. Third, a significant increase in cash financing is needed to support the more ambitious PRSPs. In principle, it should be easier to alter the direction and make up of new financing. But some commitments already made or likely to emerge could absorb a significant part of new aid commitments. This includes the response to the Tsunami disaster in 2006 and 2007, debt relief for Iraq and Nigeria, and possibly for Sudan. Collective monitoring will help ensure that planned aid commitments are delivered, and that adequate cash financing is made available to support PRSPs in the poorest countries.

10. **The World Bank will work closely with the DAC Secretariat and other partners to ensure that there is an effective international mechanism in place for monitoring, reporting, and following up on the delivery of aid commitments**. The World Bank already monitors delivery of aid commitments and tracks incremental ODA using existing DAC data definitions, classifications, and coverage. Planned increases in aid volumes will raise three issues: (a) what ODA components are to be monitored; (b) how each of the components (including cash financing) should be defined; and (c) the appropriate baseline against which commitments and their delivery should be monitored. In collaboration with the DAC Secretariat, the Bank will strengthen mechanisms for monitoring and follow-up on implementation of aid commitments, building on DAC efforts under way and on the work of the Global Monitoring Report.

11. ***Proposed Actions***. The initiative would involve the following actions:

(a) Agreeing on the components of ODA (including baseline and definitions) to be monitored: this would include a breakdown by regions (e.g. Africa), by type such as special purpose grants (which include debt relief, humanitarian/emergency assistance, administrative overheads, and technical cooperation) and cash financing; as well as spending on specific thematic priorities specified in the G8 Action Plan (such as Education for All, HIV/AIDS, malaria, infrastructure).

(b) Developing a monitoring process for aid flows that would combine data reported by donors and recipients, improve the timeliness of the data and enable a forward tracking of aid supply. This tracking process would also draw on what recipient countries report that they receive (in the case of Africa, it would build in particular on reporting under the Strategic Partnership with Africa as well as on the dialogue established between African countries, donors and multilateral organizations in the Africa Partnership Forum).

(c) Conducting joint reporting on recent developments in aid flows, including to Africa, at the DAC High Level Meeting (through the DAC annual Development Cooperation Report) and the Development Committee, on the basis of which follow-up actions could be agreed upon by the donor community. The Global Monitoring Report would be the main vehicle for reporting and analyzing aid flows at the Spring Meetings.

III. STRENGTHENING MODALITIES FOR INNOVATIVE FINANCING AND AID MOBILIZATION

12. In parallel with efforts to mobilize and deliver additional ODA and to enhance coordination to ensure the effective use of aid flows, donors have continued to explore a range of mechanisms for mobilizing additional finance to support an accelerated effort to meet the MDGs. This includes innovative financing proposals such as the International Finance Facility (IFF) and taxes, which raise practical issues of implementation and governance that are explored in this section.

A. Debt Relief

13. Additional debt relief can be a means to not only improve long-term debt sustainability, but to augment resources for MDG financing. The G8 has proposed that debt relief to completion-point heavily indebted poor countries (HIPCs) be augmented, leading to 100% cancellation of their debt to IDA, IMF, and the African Development Fund (AfDF). This proposal, which is under discussion,[4] could entail total debt forgiveness of at least $57 billion, to be covered dollar for dollar by donor payments to IDA and the AfDF, and mostly by internal resources in the case of the IMF. If fully financed as promised, debt forgiveness would provide additional resources for allocation to poor countries on the basis of performance.

B. Innovative Financing Mechanisms: Update

14. **The IFF and the IFFIm**. The U.K. Government's proposal to create an International Finance Facility is based on two basic ideas: frontloading aid (spending money now for critical development investments to reach the MDGs); and using off-budget donor commitments (in response to fiscal constraints facing donors that have pledged to increase ODA). Details on the IFF, and on the proposed pilot IFF for Immunization (the IFFIm), were included in recent papers to the Development Committee.[5] The IFFIm would raise frontloaded, reliable funding over a number of years to expand global immunization efforts to help achieve the child mortality MDG by accelerating production of new and existing vaccines and strengthening capacity to deliver vaccines.

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[4] The G8 Debt Relief Proposal: Assessment of Costs, Implementation Issues, and Financing Options, SecM2005-0466, September 6, 2005.

[5] Moving Forward: Financing Modalities Toward the MDGs, DC2005-0008/Add. 1, April 14, 2005; Aid Effectiveness and Financing Modalities, DC2004-0012/Add.1, Sept. 29, 2004.

15. On August 2, Eurostat determined that IFFIm bonds "should be recorded as debt of a non-government unit and not be imputed to the donor governments"; and that donor contributions should be recorded "at the time the actual payments by donors are to be made."[6] Eurostat noted that its decisions on the IFFIm "do not set any precedents for the IFF." Eurostat's positive decision opens the door for interested EU donors to make off-budget pledges of future ODA streams to the IFFIm, and for implementation of the IFFIm. It also allows work to move forward, and in due course for interested EU donors to request a Eurostat decision, on the full IFF. On September 9, the UK announced IFFIm contribution pledges totaling about $273 million per year for 20 years from the UK, France, Italy, Spain and Sweden.

16. **Advance Market Commitments**. There has been growing international interest in the potential for advance market commitments (AMCs) for vaccines, which could complement the IFFIm program to strengthen global immunization efforts. Under an AMC, donors would guarantee a set envelope of funding at a given price for a new vaccine that meets specified requirements. AMCs are designed to counter the disincentive for manufacturers to invest in vaccines needed in developing countries, ensuring an early market for target vaccines and thereby encouraging research, development and scale-up.

17. In April, the Center for Global Development published the report of its AMC working group. In May and June, the Bank convened preliminary consultations between representatives of industry, the G7 and public-private partnerships to further explore whether AMCs could work as an innovative financing mechanism to foster research, development and the production of vaccines for developing countries. In June, G8 Finance Ministers asked Italian Finance Minister Siniscalco to consult the relevant institutions, governments and industry, with the aim of developing concrete proposals by the end of 2005.

18. **Blending arrangements.** Blending arrangements can provide innovative ways to leverage current aid flows to meet the MDGs and serve to achieve any target level of concessionality, from market to grant terms, by combining grants and financing with different terms and characteristics. Blending can play an important role in three areas: (i) in poorest countries, a blend of concessional loans and grants can help scale up investment to meet the MDGs without undermining debt sustainability; (ii) in middle-income countries, especially those with large pockets of poor people, significant social infrastructure financing requirements, and important fiscal and debt constraints, blending can be used to give impetus to the MDG agenda and finance global and regional public goods; (iii) in "gap countries", i.e. countries not creditworthy for IBRD or other non-concessional borrowing , and with limited capacity to carry MDB debt, blending can help address development financing needs that are inadequately met in the current system.

19. The Bank is exploring the use of blending arrangements in gap and middle-income countries as part of a larger work program aimed at strengthening cooperation

[6] CMFB Opinion concerning the recording of the International Finance Facility for Immunisation (IFFIM), 29 July 2005.

between development partners in supporting development in these countries. Further work and consultations are ongoing with the aim to develop more specific proposals.

C. Innovative Financing Mechanisms: Airline Ticket Taxation Proposals

20. In April 2005, the Development Committee noted that "potential participants believe that global tax mechanisms to finance development may be feasible and desirable, while other members do not", and "invite[d] the Bank and Fund to deepen their analysis of the most promising nationally applied and internationally coordinated taxes for development for the Annual Meetings, as an input into the consideration of a pilot case."

21. In June 2005, the "Berlin Declaration" proposed a "solidarity contribution levied on plane tickets … to combat hunger and poverty and finance global sustainable development, *inter alia*, health programs including the fight against HIV/AIDS and other pandemics." The Berlin Declaration was supported by the Governments of Algeria, Brazil, Chile, France, Germany and Spain and presented at the FFD dialogue in New York in June of 2005.

22. In parallel, European Finance Ministers focused on aviation-related measures, especially flight departure taxes, as a way to increase ODA. At the ECOFIN Council meetings of May 23-24 and of June 7, a possible solidarity levy on airline tickets was discussed. On June 15, the Commission produced a technical analysis of such a levy.[7] The airline ticket tax has been discussed at the ECOFIN's informal meeting on September 9-10.

23. **Berlin Declaration proposal**. The proposed levy on airlines tickets presented in the Berlin Declaration would comprise the following elements:

(a) **Base**. The levy would apply to plane tickets issued to passengers departing from airports located in participating countries. Passengers in transit would be exempted.

(b) **Rates**. Each participating country would be able to differentiate between first/business and economy class tickets as well as between domestic and international flights, taking into account different capacities of developed and developing countries and national priorities, and the need to minimize impacts on airlines, the tourism industry and travelers.

(c) **Collection**. Airline companies would be responsible for collecting the tax, which would, in practice, be added to the fees and charges already part of the plane ticket final price. Airlines would transfer the proceeds directly to a designated account.

(d) **Cooperation**. The levy would be established by each participating country in accordance with its own laws. Voluntary coordination would take place between participating countries as to the rate, modalities and allocation of revenues.

[7] Commission Staff Working Paper: An analysis of a possible contribution based on airline tickets as a new source of financing development, June 2005, SEC (2005) 733.

National governments would remain responsible for the monitoring and the ultimate enforcement of the mechanism.

24. **Assessment of the proposal under the Bank-Fund framework**. The aid financing paper for the Spring Meetings[8] proposed a framework for the assessment of proposals on taxes to finance development, based on five criteria: revenue adequacy, efficiency, equity, ease of collection, and minimum required coalition size. An airline ticket tax performs reasonably well against these criteria.

25. First, estimates of the revenues generated by an airline ticket tax point to the possibility of substantial flows[9], even though the levy on airline tickets would be proportionately quite small.

26. Second, aviation currently escapes broad-based taxes in many countries (see Annex 1 on the economics of the aviation tax), which provides an argument for taxing airline tickets on the grounds of economic efficiency.[10] Expanding the existing broad-based taxes to include omitted sub-bases is preferable to increasing the rate of an existing broad-based tax. An overview of the economics of aviation taxes prepared by the Staff of the International Monetary Fund is presented in Annex 1.[11]

27. Third, rates can be differentiated to ensure equity in the application of a ticket tax: it can be made progressive by being levied at a higher rate on business and first class passengers than on economy class passengers; rates can be set to reflect differences in income between developed and developing countries; and to avoid penalizing large countries, rates could be also differentiated between domestic and international flights, as is now done in the UK.

28. Fourth, given the relatively small number of companies involved and the existence of arrangements for the collection of departure taxes and airport security fees, an airline ticket tax is expected to be relatively easy to collect, as detailed below.

29. Finally, while universal participation would increase the revenue potential and the overall development impact of the mechanism, it would not be necessary. Assuming that the tax is levied at a low rate, it is unlikely that non-participation by some would have significant impacts on the choice of origin or destination of trips.

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8 Moving Forward: Financing Modalities Toward the MDGs, DC2005-0008/Add. 1, April 14, 2005.

9 The Berlin group estimates that a 5 euro contribution on all plane tickets worldwide with a 20 euro additional surcharge on business and first class would annually yield up to euro 10 billion. The European Commission estimates that, with a tax rate of 5 euro on intra-community flights and 10 euro on international flights, applied EU wide, expected revenues would be about euro 2.7 billion per year.

10 Some have argued for taxing airline tickets in order to correct externalities such as the impact of air travel on greenhouse gas emissions or local air pollution. However, key externalities do not vary in direct proportion to the number of airline passengers. Greenhouse gas emissions are proportional to fuel consumption; local air pollution and noise externalities are roughly proportional to the number of takeoffs and landings, and to plane size.

11 See also the forthcoming IMF paper on the topic, "The public economics of global indirect taxes on aviation".

30. **Potential impact**. One important aspect of an airline ticket tax will be its impact on affected groups, notably, the airlines. The effect of a departure tax on airline revenues depends on the price elasticity of demand for air travel and on the extent to which the airlines adjust pre-tax prices to reflect the tax.[12] Price elasticities of demand vary significantly between business and leisure travelers, short- and long-distance flights, and domestic and international flights, so the impact of the tax on specific airlines will depend on what portion of an airline's revenues come from these segments of the market. A recent report commissioned by the Canadian Department of Finance estimated fare elasticities for air travel (see Annex 2). Mean estimates ranged from –0.265 for long-haul international business passengers to –1.52 for short-haul leisure travelers. At any given rate, airlines that receive a higher proportion of their revenues from international business travelers thus will be less adversely affected by the tax.

31. Overall, the impact of the proposed tax on airline revenues will likely be a small reduction of between 0.5% and 1%, assuming a ticket tax of no more than 1% of ticket price. As the demand for air travel is projected to grow by 5% yearly over the next decade, the impact of the tax would be absorbed in less than a year.

32. The impact on individual carriers will also depend on how many and which countries adopt an airline ticket tax. Carriers with a greater share of their flights originating in countries that impose a tax will be more affected than carriers whose flights originate mostly in countries that do not impose a tax.[13]

33. To move forward with a uniform airline ticket levy, framework arrangements would be agreed multilaterally, either informally or formally as a treaty. They would be adopted into national law in each participating State. Key elements would include agreement on tax rates and collection provisions; procedures for adjusting rates; interest and penalty rates; procedures for assessment, registration, collection, payment, enforcement, and dispute resolution.[14] Airline companies would be responsible for accounting, paying and reporting taxes. Revenue collection would normally be undertaken at the national level by participating governments, and used in line with agreed aid priorities. Alternatively, the funds could be channeled through existing multilateral mechanisms.

D. Implementation and Governance Issues for New Financing Modalities

34. The most effective use of new proceeds for development would be to channel them through existing mechanisms, in particular, multi-purpose, flexible channels with a

[12] For example, if ticket prices are raised by the amount of the tax, airline revenues will rise, but normally by less than the amount of the tax revenue to be collected. Because the elasticity of total revenue with respect to price equals 1 plus the price elasticity of demand, a price elasticity of –0.5 would imply that revenues would rise by half of the amount of the tax to be collected.

[13] This effect will occur even if the tax does not alter passenger choice of flight origin or destination. The likelihood that the tax will affect choice of origin or destination seems low: the costs of departing from a different country than one's country of residence are likely, in most cases, to outweigh the tax saving.

[14] The option of establishing a voluntary contribution mechanism using airline tickets is not considered here, as it would entail more complex administrative arrangements to implement and would result in only limited predictability of flows. In addition, it is not clear if a voluntary contribution approach would be satisfactory for donor governments as it would not be classified as ODA.

minimum of earmarking but with strong requirements for monitoring and demonstration of results. Flexibility and harmonization in the use of funds is considerably hampered to the extent that they are restricted to particular countries or specified end uses. This is a substantial problem with the recent growth of specialized facilities in recent years. On the one hand, it may be easier to attain broad-based public acceptance new financing mechanisms if proceeds are earmarked. On the other hand, these possible advantages need to be carefully weighed against the rigidities, distortions and risks of undermining country ownership that accompany earmarking.

Core Principles

35. ***Efficiency***. The creation of new institutions, structures or procedures should be avoided; existing institutions and processes should be relied on to the extent possible to ensure efficiency and harmonization of aid delivery. In particular, the existing aid architecture should not be made more complicated by any additional burden or transaction costs for aid recipients, who are already managing a multiplicity of requirements from donors and other sources of aid. To minimize the cost of administration of global tax revenues, allocations should be made to and through existing aid institutions, relying on the assurance provided by known governance standards, policy frameworks and implementation capability, and with minimal conditionality beyond specified basic standards such as untied procurement.

36. ***Country Ownership.*** It is important to not undermine country ownership of the development agenda. Funding specific MDGs may make sense if limited funds are available in the near term. However, the use of earmarked funds can cause distortions at the country level in terms of resource allocation, pressure on implementing capacity, increased transaction costs, and misalignment with country-owned mechanisms such as PRSPs. At the country level, incremental funding must continue to be based on implementation capacity (including additional support for capacity building), fiscal space and sustainability, and it must be introduced as an integral part of national planning and budgeting mechanisms. It may be noted that, if tax revenues are earmarked to specific uses, it will be all the more important to have them managed by institutions capable of combining them with other flows for complementary purposes and to achieve broad MDG goals. This will help to avoid privileging a particular MDG at the expense of the others or of broader development achievements.

37. ***Predictability***. To support predictable use of aid flows by recipients, allocations should be made with the assurance of a specified baseline of flows, adjustable upwards if revenues materialize, for a specified period, subject only to continued achievement of some basic standards of performance. This would take advantage of the core attribute of flows from a relatively steady source such as an airline ticket levy, which can provide greater predictability of financing over a longer period of time.

38. ***Transparency***. To ensure public acceptance and support of the tax, clear information must be made available about the use of tax revenues. Reporting arrangements should foster the ability to make a direct link between the ways tax revenues are spent and development outcomes. This will not necessarily require specifying developmental uses, such as for health or education, but will require that implementing agencies have credible and supportable programs.

39. ***Additionality.*** New financing mechanisms must meet the test of additionality. Substitution effects can be a risk if bilateral donors switch their resource allocation to new funding mechanisms while their overall support to development spending, or to specific sectors for earmarked funding, does not increase. The allocation of new financing mechanisms to development uses must not displace development spending from traditional sources. Public disclosure of these flows and their uses, along with continued disclosure of overall ODA and its composition, will help spotlight the importance and level of additionality.

40. ***Conditionality.*** Any new financing mechanism raises the question of whether and what additional conditionality would be required in the provision of financing. In keeping with the principle that such financing would be channeled through existing delivery mechanisms, there would be no strong case for separate conditionality. Donors would have, however, to be convinced of and buy into the conditionality and results framework of the delivery mechanisms to be used.

Implementation issues

41. No new implementation or governance issues would arise if the revenues mobilized were used to support national aid budgets, and channeled through existing national mechanisms – as currently proposed with the airline ticket levy. If the revenues were commingled or mobilized using multilateral mechanisms such as the IFF, governance arrangements on the use of proceeds would have to be specified.

42. ***Governance Body***. A governance body would need to assume responsibility for basic allocation decisions – what funding proportions and levels should go to which development institutions – and any other core elements for which adoption into domestic law is impractical. The governance body could be an existing institution or a new entity, and could be established formally as a legal entity or informally as an alliance or advisory group. It would rely on the implementing agencies for specific programmatic and project decisions.

- Membership. Donor governments would normally be the primary members making governance decisions. However, settling the membership structure will inevitably give rise to fundamental tradeoffs. For example, inclusion of recipient governments, implementing agencies, and possibly civil society representatives would make the governance body more fully representative but possibly less efficient.

- Rules of the road. The use of implementing agencies removes the need for a detailed policy framework, although some basic principles could be established by the governance body, such as providing funding over the longer term to ensure predictable financing, or requiring untied procurement.

43. ***Executive Body***. A secretariat will be needed to provide basic administrative support, notably for the periodic meetings of the governance body. The role of the secretariat may be more or less substantial depending on the frequency of meetings of the governance body and the extent of its authority and responsibilities; a minimal secretariat would help ensure that funds are used for development purposes rather than to cover administrative costs. Similarly, the extent of the financial management/oversight

functions will depend on whether revenues are collected by donor governments or paid directly into a commingled fund for disbursement to implementing agencies.

44. ***Implementing Agencies*** would be selected by the governance body, and allocations made and adjusted on a periodic basis with a view to long-term funding predictability. Implementing agencies should work on the basis of country-owned strategies or country-based application processes.

45. There are no perfect models or precedents for the governance of innovative financing mechanisms; the optimal design of detailed governance arrangements will have to be based on the particular circumstances. Existing organizations and partnerships can provide useful guidance as specific governance arrangements are considered– a few examples include:

- The Global Environment Facility provides an example of core funds being provided to <u>implementing agencies</u> to supplement their core work.
- The Education for All/Fast Track Initiative (EFA/FTI) is an example of a <u>country-owned, results-based</u> program; it is intended to provide long-term funding for education programs against specified education outcomes.
- Creating a lean <u>governance body</u> on which multiple perspectives are nonetheless represented is a challenge. The Board of the Global Alliance for Vaccines & Immunization, for example, has only 12 members but they represent the entire immunization community: donor and recipient countries, the vaccine industry in industrial and developing countries, multilateral institutions, NGOs, private and public health institutes, and foundations. Board members represent a constituency and rotate periodically.
- To provide <u>funding through a development institution</u> with a comprehensive agenda, such as IDA or the other multilateral concessional windows, parallel trust funds could be used to increase financing amounts for projects meeting specified purposes. An example is the Policy and Human Resources Development program, through which Japan supports recipient countries in the preparation, implementation and cofinancing of World Bank loans, credits and grants. Similarly, discussions are ongoing between DFID and IDA to create a partner fund to provide scale-up financing through IDA for agreed purposes. Close affiliation with the multilateral institutions would help ensure performance-based approaches and minimize fragmentation and transaction costs.

E. Improving the Coherence of New Aid Financing

46. The expansion of aid volumes and commitments since Monterrey and work on new modalities could lay the basis for an aid architecture that could be more responsive to development needs, including the financing of the MDGs.

47. However, there are two important tensions in the aid architecture that are likely to intensify and will need to be carefully managed. The first tension is between the centrality of country-based approaches and the push for progress on specific MDGs, which can undermine country ownership and increase fragmentation of financing. A second tension is between the importance of performance-based approaches and

opportunities for scaling-up. Three circumstances in which aid can opportunistically help scale up efforts to meet the MDGs include: (a) opportunities to make a "big push" in high performing countries that can productively absorb large increases in aid; (b) exceptional support in turnaround situations with high risk but potentially high return, including post-conflict, fragile States and incipient reform cases; and (c) scaling up regional investments that represent a clear opportunity to achieve regional public goods.

48. ***Proposed Actions***. Against this background, the Bank could take the following actions to support effective and more coherent deployment of new and existing aid flows:

(a) Strengthen support for Poverty Reduction Strategies (PRSs) as a platform for more ambitious country planning in scaling-up efforts to reach the MDGs, including the incorporation of "quick-wins".

(b) Support targeted sector interventions and push on selected MDGs. As long as they are aligned with PRS processes, global initiatives on thematic goals can facilitate the initiation and development of sectoral scale-up plans and provide a channel for donors to engage in sectoral policy dialogue and for partner countries to access international expertise without a proliferation of sectoral activity by bilateral donors.

(c) Ensure that additional bilateral funding and innovative financing revenues are closely coordinated with IDA. This could increase leverage, promote a country- and performance-based approach, and minimize fragmented approaches.

(d) Explore possibilities for a new financing mechanism anchored in the Bank (a "catalytic" or "venture capital" fund). This fund could address the special opportunities noted above, including for high-performing countries, turnaround situations, and regional investments, while maintaining country ownership and integrated expenditure management systems supported by IDA. To ensure that such a fund operates efficiently, the specific circumstances and criteria under which its financing could be used would have to be precisely delineated.

(e) Revamp the Consultative Group mechanism to become annual "resources and results meetings," thus raising the scope of these meetings to address the sequencing of aid taking into account absorptive capacity, strengthening partnerships on the MDG agenda and tightening the link between resources and results. Consultative Groups would also monitor progress in country-level implementation of Paris targets and take necessary follow-up actions.

(f) Establish mechanisms for donor consultations, in cooperation with DAC and leading bilateral agencies[15], so as to improve predictability and coherence, including through indications of the levels, channels and forms of aid available from individual donors.

[15] Such mechanisms could also build on the dialogue established in the Africa Partnership Forum.

IV. MANAGING FOR RESULTS AND FOLLOWING UP ON THE PARIS HIGH-LEVEL FORUM

49. The challenge of achieving the MDGs calls for increased development assistance as well as enhanced effectiveness in the use of development resources. Since Monterrey, a renewed focus on aid effectiveness and results has been at the forefront of the global development agenda. The Rome High-Level Forum on Harmonization in 2003, the Marrakech Roundtable on Managing for Development Results in 2004 and the second High Level Forum on Harmonization in Paris in March 2005 brought together all stakeholders – bilateral agencies, multilateral institutions, developing country partners and civil society – to address the aid effectiveness agenda through better alignment and harmonization and an enhanced focus on results.

A. Managing for Results

50. Implementation of the Bank-wide agenda on better managing for results focuses on actions in three areas:

(a) in countries, where development results are achieved, the Bank is supporting countries in strengthening national strategic planning (including for poverty reduction strategies) and building results-based public sector management, statistical capacity, and monitoring and evaluation systems;

(b) in the World Bank, there is focus on results in all Bank strategies, instruments, incentives, and reporting systems (including the mainstreaming of results-based Country Assistance Strategies, simplification of documentation and procedures for major lending instruments, the establishment of a two-tiered Results Measurement System for IDA14, and the use of Key Performance Indicators in Strategic Performance Contracts);

(c) across development agencies, strong partnerships have been established through the MDB Working Group and, more recently, through the MDB/OECD-DAC Joint Venture on Managing for Development Results, to harmonize results-based approaches and better coordinate support to strengthen country capacity to manage for results. In addition, there is now agreement on a medium-term global action plan to strengthen international statistical systems.

51. Prospects for additional aid flows put an even higher premium on further progress for measuring, monitoring, and managing for results. Strengthened country capacity to manage for results and global partnership will be a prerequisite to ensure the most effective use of additional aid flows, and improved accountability and transparency. Working closely with the Development Assistance Committee (DAC) of the OECD, the UNDG and the MDBs, the World Bank will continue to lead and contribute in this effort, both globally and at the country level.

52. ***Proposed Actions***. This effort would involve the following set of actions:

(a) Support country efforts to strengthen results-oriented reporting and monitoring frameworks in order to prioritize, monitor, and evaluate their poverty reduction strategies and national development plans as appropriate. In collaboration with other development partners, mount an effort in at least 10 countries in Africa, and two countries in each of the other five Regions, to collect baseline and comparative information in key areas of public service delivery.

(b) Build country capacity to measure and manage for results by scaling up present efforts to strengthen statistical capacity, in particular through supporting the efforts of PARIS21 and the World Bank's Trust Fund for Statistical Capacity Building to assist all low-income countries in the design and implementation of a national strategy for the development of statistics. There will be focus on 15 countries that are willing to invest in their capacity to produce, analyze and use better data. To strengthen demand, progress in implementing country-based results systems will be a factor in lending levels.

(c) Mainstream results-based CASs that (a) establish a results framework linking Bank resources and programming more explicitly to country priorities, (b) strengthen monitoring to steer CAS implementation toward agreed results, and (c) increase emphasis on strengthening country capacity to manage for results.

(d) Continue to aggregate data on country performance and quality and composition of donor support in the annual Global Monitoring Report.

(e) Expand and strengthen the international partnership on statistical work including preparations for new, priority, global data gathering efforts and extend the International Household Survey Network. The goal is to cut by half the gap in country coverage of key MDGs and IDA14 results indicators (from roughly 30% currently in Africa to 15%).

(f) Support the impact evaluation of Bank-funded programs (for example, school-based management, slum upgrading, conditional cash transfers) under the Bank's new "development impact evaluation" initiative (DIME). These evaluations will assess whether the observed outcomes of a program can be attributed to the financed program by comparing them to a counterfactual situation, enabling policymakers and the donor community to monitor outcomes and learn about the development effectiveness of specific interventions.

(g) Foster global partnership in managing for results by encouraging harmonization of monitoring and evaluation systems and reporting requirements among donors, along with increased commitment and coordination of support to strengthen country capacity. Develop and maintain, jointly with bilateral and multilateral donors, Sourcebook on emerging good practice in managing for results. In cooperation with the DAC, the MDBs, and the United Nations system, lead the preparation of the Third International Roundtable on Results to be held in fall 2006.

B. Aid Alignment and Harmonization

53. In Rome in 2003, the Bank and other donors committed to align development assistance with partners' strategies, help partners improve their systems, harmonize donors' policies and procedures, and implement principles of good practice in development cooperation. Following two years of further consideration and country-level experimentation with planning and delivering aid through more harmonized approaches, the second High-Level Forum was held in Paris in February-March 2005, to

assess progress. Sixty partner countries (more than twice the number that attended Rome), 30 donor countries, and 30 development agencies attended the meeting and endorsed a detailed framework of harmonization and alignment embodied in the Paris Declaration on Aid Effectiveness.

54. In addition to 56 detailed commitments, the Paris Declaration contains 12 indicators to monitor progress with respect to ownership, alignment, harmonization, results and mutual accountability. After the Paris Forum the Working Party on Aid Effectiveness, the partnership of donors and partner countries hosted by the OECD-DAC, work urgently to develop and agree on targets associated with the 12 indicators, completing its work in July and communicating these to developing countries' and donor countries' officials world-wide in early August. The indicators and targets identified through this process are designed to track and encourage progress at the global level among over 100 countries and agencies that have agreed to this Declaration. Equally important will be tangible efforts on the ground, to learn from and replicate good practice. As of September 1, there is a full consensus among all participants of the Paris High Level Forum on the indicators and targets (see annex 3), subject only to a reservation at this stage by one donor on the methodology for assessing quality of procurement systems and the quality of public financial management reform programs. The concluding statement of the mid-September UN General Assembly High-Level Plenary Meeting welcomed recent initiatives, including the Paris Declaration on Aid Effectiveness, and resolved to take concrete, effective and timely action in implementing all agreed commitments on aid effectiveness, with clear monitoring and deadlines.

55. It was further agreed in Paris that two rounds of monitoring will be undertaken between now and 2008 when a third High Level Forum on Aid Effectiveness will take place. The first round is to be undertaken in 2006 and the second in 2008. It has been proposed that Ghana host the next High Level Forum.

56. ***Proposed Actions***. The World Bank expects to continue to play a key role in supporting implementation of harmonization and alignment, guided by the Paris Declaration. Making progress where it counts most, at the country level, will entail actions externally in partnership with other donors and partner countries, and internally with staff across regions and networks:

(a) Externally, actions by the World Bank will include:

- Lead by example in implementing the Paris framework by doubling the number of countries to at least 30 by 2007, where the Bank is leading or is a major participant in country-level harmonization and alignment efforts.
- Collaborate with partner countries, DAC, other MDBs and other development partners to disseminate good practices and implement, monitor, and assess country-level progress toward agreed global targets on the Paris agenda.
- Work with donors in moving to country led financial- and results-management systems in ten countries by 2008.

- Promote stronger mutual accountability between the stakeholders by supporting independent evaluations of donor-country relations and the management of development assistance in six pilot countries by 2007.
- Use the Consultative Group mechanism to follow up on progress in implementing the Paris Declaration, reporting on achievements and agreement to address constraints and the way forward.
- Collaborate with DAC, MDBs, UN, and host country Ghana to organize, prepare, and oversee a Third High-Level Forum on Aid Effectiveness in 2008.

(b) Within the World Bank, actions will include:

- Review the experience of collaborative/joint CASs, drawing lessons learned from these to broaden the number of countries where similar joint work can be undertaken. World Bank contributions to country-level harmonization will be reviewed in CAS Completion Reports and described in CASs.
- Seek opportunities where the Bank can participate in cofinancing arrangements either as the lead donor, or with other donors where another donor is leading.
- Work with other interested donors in countries where this is feasible to harmonize procurement and financial management practices as a step towards aligning donor requirements with country systems.
- Undertake a review of initial experiences with harmonization and alignment at the country and sector level—on what has worked and what has not—and prepare a good practice paper reflecting these. The review would include, inter alia, experiences on collaborative/joint assistance strategies, MOUs/partnership agreements, sectorwide approaches and joint country and analytic work. A good practice note on Project Implementation Units (PIUs) has recently been completed which sets out alternative models for project management.
- Use learning events and other mechanisms to familiarize staff with harmonization and alignment approaches, Bank commitments and good practices.
- Track and report (e.g., in the Global Monitoring Report) World Bank progress in implementing the Paris Declaration, and also track the recently adopted regional key performance indicators on harmonization and alignment and use of country systems.

ANNEX 1

THE ECONOMICS OF TAXES ON AVIATION[16]

Note prepared by the Staff of the International Monetary Fund

1. Background

A global indirect tax on civil (passenger and freight) aviation has been among the most frequently mentioned possibilities for additional development finance. Such a tax is prominent in several recent international documents on the topic, both in the Landau Report (2004) written for the French government, and in the Quadripartite Report (2005) formulated by France, Germany, Brazil and Chile. The European Union is currently examining the introduction of aviation taxes for global finance purposes, but in the first instance limited to the EU area. More recently, France and Brazil have expressed interest in going ahead with a ticket tax on airfares for development purposes, in 2006, on an experimental basis.

The background for an interest in introducing a global aviation tax is the recognition that aviation today is lightly taxed, absolutely and relatively at least when compared to related activities in some regions such as European road transport. At the same time aviation gives rise to substantial global and local externalities, mainly in the form of emissions to air and noise. Three types of aviation taxes have been seriously considered: An aviation fuel tax; ticket taxes (proportional to the value of passenger tickets or cargo waybills); and departure taxes (fixed per departure and applying only to passengers, but possibly differentiated between travel classes and trip lengths). The IMF's work on aviation taxes has so far only considered fuel taxes and ticket taxes in any detail. The main reason for this is that these two are better than departure taxes at addressing externality issues. In the recent EU discussions, departure taxes are however seen as the most relevant alternative, mainly for practical and implementation reasons.

2. Current indirect taxes on aviation

Aviation fuels are currently subject to little tax, and for most countries with such taxes only domestic aviation fuel consumption is taxed. Among developed countries, the Netherlands and Japan have substantial domestic aviation fuel taxes (but no international taxes). Australia, Canada and Norway have a uniform (both domestic and international) fuel tax, while the United States has sales and state-specific aviation fuel excise taxes, all within 2-8 % of fuel prices. The Chicago Convention on International Aviation currently prohibits the taxation of aviation fuels carried by an aircraft into another country's territory. The absence of international aviation fuel taxation seems otherwise in some cases to be due to treaties that prevent such taxes. Tax competition, in any event, is likely

[16] For a more complete discussion of global aviation taxes, see *"The Public Economics of Coordinated Indirect Taxes on Aviation"*, IMF forthcoming.

to sustain low taxes on international aviation, since individual countries face the possibility that aircraft largely tank outside of their territory where taxes may be lower.

Ticket taxes (including VAT) are also relatively infrequent. No high-income country has ticket taxes on international aviation, but most European countries have VAT on domestic aviation albeit at reduced rates (except Germany which has a full rate of 16%). Some low-income countries (mainly in Latin America) have both international and domestic ticket taxes or VAT.

Departure taxes and airport charges are far more common. Their rates tend to be highest for international travelers, particularly so in low-income countries. Airport charges, and perhaps often departure taxes, must be viewed not as regular taxes on aviation but rather as charges for services provided by airports, including security services. Thus only charges in excess of costs of providing such services can be viewed as true aviation taxes.

Our data on the distribution of relevant airport and other aviation-sector costs are incomplete, and it is unclear whether the aviation sector is currently over- or under-charged. The general tendency seems to be that international aviation is undercharged in high-income countries, while domestic aviation is undercharged in low-income countries. In some high-income countries, including Australia, the Netherlands and the UK, the relevant charges may appear to be higher than airport and other aviation costs.

3. Externalities from air transport

The main externalities from air transport, as presented by the IPCC (1999), are local air pollution, carbon emissions, noise, and congestion externalities in airports. Air pollution externalities due to aviation are complex and not yet fully understood, but could be substantial. Note that carbon emissions from aviation are currently not subject to Kyoto quotas.[17] As for (subsonic) noise, this is significant largely in the vicinity of airports.

There are few good estimates on marginal externality costs of aviation. One British study (Pearce and Pearce [2002]) however indicates an average marginal cost (for Britain) equivalent to about 30 US cents per gallon of aviation fuel.

4. Principles for determining the optimal level of international aviation taxes

The marginal externality cost of aviation gives an indication of the appropriate (Pigouvian) aviation tax, under certain assumptions. Major modifications to the Pigouvian principle apply if there is distortive taxation among the relevant countries, and when airlines behave non-competitively. The effect of distortionary taxes on the optimal Pigouvian tax is unclear. Whether an aviation tax should be higher or lower than marginal externality cost in the presence of other distortive taxes depends on several factors. One is whether the taxed good is a substitute or a complement for leisure. If it is a substitute, the tax will increase the deadweight loss of the income tax and the tax should be less than marginal social damage; if it is a complement, the tax will lower the deadweight loss associated with the income tax and the tax should be higher than

[17] The European Commission, however, has recently proposed that airlines be included in Europe's emissions trading scheme for greenhouse gas emissions (*Financial Times*, July 25, 2005).

marginal social damage. A (Ramsey-type) need for tax revenue in isolation to increase optimal aviation tax beyond the Pigouvian level. Non-competitive behavior lowers the optimal tax, since it typically leads to a lower than efficient aviation output, and this inefficiency is made worse by high taxation of the sector. Whether or not the optimal aviation tax then is higher or lower than the marginal externality cost of aviation (representing the Pigou level) is then an empirical issue.

5. <u>Choice of aviation tax instrument</u>

As noted, two main alternatives for aviation taxes are fuel taxes and ticket taxes. Both have advantages and disadvantages. The main advantage of the fuel tax is that it more directly taxes the externality-causing activity, namely aviation fuel use. It is thus likely to be relatively efficient in reducing fuel use, for example by giving airlines incentives to phase out inefficient planes and keep few empty seats on flights. Its main disadvantage is that it cannot readily be differentiated between countries and traveler groups, whenever this is viewed as desirable. A main relative advantage of a ticket tax is that it can readily be made to differ between economy- business- and first-class passengers, and between countries, flight types, etc. The revenue-raising potential is generally also higher for ticket taxes, in particular since high-end passengers (with greater willingness to pay for taxes) can be targeted more effectively to pay higher taxes. The back side of the ticket tax is that it is less efficient at counteracting the externality effects. In particular, it gives airlines fewer incentives to reduce idle seat capacity or switch to more fuel-efficient aircraft. One additional advantage of the ticket tax is that it (and not the fuel tax) serves as a tax on, and thus counteracts some of the inefficiencies associated with, non-competitive behavior among airlines.

Both aviation fuel taxes and ticket taxes face potential legal problems of implementation, at least in the short run, due to various inter-country agreements for non-taxation. The departure tax, not extensively analyzed in the context of this annex, currently faces fewer legal problems. It is, however, less effective than the ticket tax in addressing some externalities associated with aviation and reducing aviation fuel consumption. Moreover departure taxes may seem less relevant for air freight representing 12% of global aviation fuel consumption, while air freight naturally is taxed by either ticket or fuel taxes.

6. <u>Revenue potential of aviation taxes</u>

Revenues for aviation taxes depend on air travel volumes to and from different countries and regions, on distributions among different countries' air carriers, and in addition on what types of taxes are imposed. Three regions dominate international aviation: North America, with 31 (36) percent of passengers (passenger kilometers); Europe, with 30 (28) percent; and East Asia and the Pacific region, with 26 (24) percent, respectively. The rest of the world (including Latin America, Africa, and South and Central Asia) represent 13 and 12 percent of passengers and passenger kilometers, respectively.

With uniform global ticket tax rates, the distribution of taxes across major regions largely corresponds to the distribution of passenger kilometers, at least when air fares are approximately proportional to distances traveled. These taxes may however be differentiated, and may then possibly be set higher for business- and first-class passengers than for economy-class passengers, and may to some degree be made to depend on trip length and on region. About 50% of global aviation passenger revenue is from business- and first-class travelers. With higher ticket tax rates for these than for economy-class travelers, more than 50% of aviation ticket taxes will be collected from the business- and first-class passenger segments.

The regional distribution of fuel taxes depends on travel volumes for different countries' airlines, as these taxes are charged to airlines and not to passengers. These volumes are roughly in line with distributions of traffic between countries. They are however slightly higher for North American and European airlines, as these have a larger than proportionate traffic on international routes to third countries.

Aviation tax revenue will depend on the tax base and the tax rate in each case. With a departure tax of 5 Euros (6 US dollars) per departure (as has recently been suggested in the European Union), and with current global air traffic volumes (about 1.8 billion departures), the annual revenue potential is approximately 11 billion US dollars. A departure tax of 20-30 Euros for business- and first-class passengers has also been suggested. A 20 Euro (25 US dollar) tax for business class globally would raise about 6-7 billion US dollars. A fuel tax of 20 US cents per gallon would raise about 10 billion US dollars, and the same would be raised by a uniform ticket tax (on all air tickets) of about 2.5%. An advantage of the latter two taxes (relative to departure taxes) is that air freight could be taxed alongside passenger traffic. It must also be noted that developing and emerging economies represent about 20% of global aviation activity. Exempting these from aviation taxes would thus reduce the global revenue potential by about 20%, in all three cases (fuel taxes, ticket taxes and departure taxes).

7. Administration and compliance

Technically, adding taxes to either fuel consumption or ticket issues represents few fundamental problems. Fuel taxes can be collected from a small number of airlines, and ticket taxes can, if necessary, be collected at several points in the case of multi-leg flights. Departure taxes would be collected at point of departure for passengers. The main problems would rather be in terms of incentives to collect the taxes in the individual country, when it is known that possibly none of the proceeds are to be retained in the country.

AIR TRAVEL DEMAND ELASTICITIES

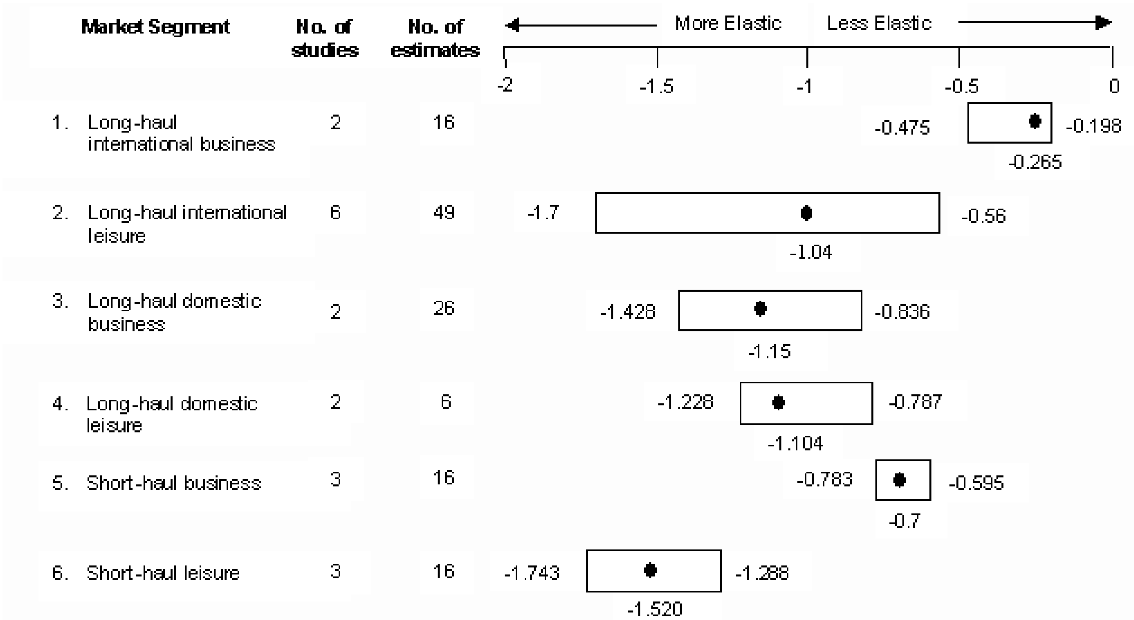
Several studies reviewed by the staff of the EU Commission on the aviation industry concur on overall price elasticities of demand between –0.6 and –1.1. Other studies, reported by the IMF and the UK Department of Transportation, yield overall elasticities between –0.5 and –0.7, and –0.8, respectively.

A recent report commissioned by the Canadian Department of Finance (Gillen, Morrison and Stewart, 2003) presents estimates of fare elasticities for six markets for air travel: business and leisure travel; long-haul and short-haul travel; and international and North American long-haul travel. The estimates are based on 21 Canadian and international studies of own-price elasticities of demand for air travel.

The report concludes that, since the availability of substitutes for air transport diminishes with distance traveled, it is expected that the demand for air transport will be less elastic for longer flights than for shorter flights. Further, international travel tends to be spread over more time than domestic travel, so that the airfare is a smaller proportion of overall trip costs, which makes international travel less sensitive to changes in ticket prices. In addition, leisure travelers are more likely to postpone trips to specific locations in response to higher fares, or to shop around for those locations offering more affordable fares. Consequently, it is expected that the demand for air transport for leisure will be more elastic than business travel.

Summary results from the report are reproduced in below. Median elasticity values (black dots) differ significantly by type of traveler, travel distance and domestic versus international routes, and confirm the existence of distinct air travel markets. They generally accord with expectations that the demand for air transport should be less elastic for business than for leisure travelers, and less elastic for flights of longer distances, notably for international travel. Based on available studies, however, markets for business travel do not show a consistently increasing responsiveness as distance traveled becomes shorter. The chart also shows, for each market, the range of elasticity values within which one-half of the estimates lie. An important caveat to the interpretation and use of these estimates is that the median and range of values for some of the distinct markets for air travel are based on a relatively small number of estimates and studies.

Price Elasticities of Demand



ANNEX 3

PARIS DECLARATION INDICATORS /TARGETS

Indicators		Definitions / Qualifying criteria	Targets for 2010	
1	**Operational development strategies**	Partner countries have operational development strategies when they have **substantially** developed (score an 'A' in CDF methodology) or **largely developed** (score a 'B') operational development strategies.	**Target**	**At least 75% of partner countries** have operational development strategies.
2a	**Reliable PFM systems**	Partner countries increase their score against the PFM scale of performance. The PFM scale of performance is based on the CPIA assessment and ranked from 1 (very weak PFM systems) to 6 (very strong) in half point (0.5) measures.	**Target**	**Half of partner countries** move up at least one measure (i.e. 0.5 points) on the PFM/CPIA scale of performance.
2b	**Reliable Procurement systems**	Partner countries increase their score against the Procurement scale of performance. The Procurement scale of performance is ranked from 'A' (systems fully achieve good practice) to D (systems do not achieve good practice).	**Target**	**One third of partner countries** move up at least one measure (i.e. from D to C, C to B or B to A) on the four-point scale used to assess performance for this indicator.
3	**Aid is reported on budget**	Additional technical guidance to be developed by the WP-EFF on coverage of this indicator	**Target**	**Halve the gap** — halve the proportion of aid flows to government sector not reported on government's budget(s) (with at least 85% reported on budget).
4	**Coordinated capacity development**	Additional technical guidance to be developed by the WP-EFF on operational definition of "coordinated programmes" and "technical cooperation."	**Target**	**50% of technical cooperation flows** are implemented through coordinated programmes consistent with national development strategies.
5a	**Use of PFM systems**	Partner countries with a **score of 5 or above** on the PFM/CPIA scale of performance (see Indicator 2a)	**Target**	**Reduce the gap by two-thirds** – A two-thirds reduction in the proportion of flows to the public sector not using partner countries' PFM systems.
	(% of aid flows)	Partner countries with a **score between 3.5 and 4.5** on the PFM/CPIA scale of performance (see Indicator 2a)	**Target**	**Reduce the gap by one third** — A one-third reduction in the proportion of flows to the public sector not using partner countries' PFM systems.
5a	**Use of PFM systems**	Partner countries with a **score of 5 or above** on the PFM/CPIA scale of performance (see Indicator 2a)	**Target**	**100% of donors** use partner countries' PFM systems.
	(% of donors)	Partner countries with a **score between 3.5 and 4.5** on the PFM/CPIA scale of performance (see Indicator 2a)	**Target**	**90% of donors** use partner countries' PFM systems.
5b	**Use of Procurement systems**	Partner countries with a **score of 'A'** on the Procurement scale of performance (see Indicator 2b)	**Target**	**Reduce the gap by two-thirds** — A two-thirds reduction in the proportion of flows to the public sector not using partner countries' procurement systems.
	(% of aid flows)	Partner countries with a **score of 'B'** on the Procurement scale of performance (see Indicator 2b)	**Target**	**Reduce the gap by one third** — A one-third reduction in the proportion of flows to the public sector not using partner countries' procurement systems.

	Indicators	Definitions / Qualifying criteria	Targets for 2010	
5b	**Use of Procurement systems**	Partner countries with a **score of 'A'** on the Procurement scale of performance (see Indicator 2b)	**Target**	**100% of donors** use partner countries' procurement systems.
	(% of donors)	Partner countries with a **score of 'B'** on the Procurement scale of performance (see Indicator 2b)	**Target**	**90% of donors** use partner countries' procurement systems.
6	**Parallel PIUs**	**PIU** — dedicated management units designed to support donor funded projects or programmes. **Parallel PIU** – PIU created outside the existing structure of the national implementing agency (e.g. ministry or other agencies) or which duplicate or recreate ministry functions and capabilities.	**Target**	**Reduce by two-thirds the stock of parallel PIUs**
7	**Predictability**	Additional technical guidance to be developed by the WP-EFF.	**Target**	**Halve the gap —** halve the proportion of aid not disbursed within the fiscal year for which it was scheduled.
8	**Aid is untied**	Data drawn from reporting by DAC donors to the annual DAC questionnaire.	**Target**	**Continued progress over time.**
9	**Programme-based approaches**	Programme-based approach (PBA) as defined in Paris Declaration and categorised as follows: ▪ National support (general budget and balance of payment support). ▪ Sector support (budget support at sector level and projects integrated in sector-wide approaches). ▪ Other forms of PBAs. Additional technical guidance to be developed by the WP-EFF.	**Target**	**66% of aid flows** are provided in the context of programme based approaches.
10a	**Joint missions**	**Donor missions to the field** — are missions undertaken by officials to an aid recipient country and that include a request to meet with officials from the country of destination excluding workshops, conferences etc.	**Target**	**40% of donor missions to the field are joint.**
10b	**Joint country analytic work**	**Country analytic work** — country analytic work is defined to include: ▪ Diagnostic reviews (e.g. CPAR). ▪ Country or sector studies and strategies. ▪ Country or sector evaluations and discussion papers.	**Target**	**66% of country analytic work is joint.**
11	**Performance assessment frameworks**	Partner countries have transparent and monitorable performance assessment frameworks when they have **substantially** (score an 'A' in CDF methodology) or **largely developed** (Score a 'B') good practice in this area.	**Target**	**Reduce the gap by one third —** Reduce the proportion of countries without transparent & monitorable performance assessment frameworks by two-thirds.
12	**Mutual accountability**	**Mutual assessments** include independent assessments and can draw from South-South learning.	**Target**	**100% of partner countries** have mutual assessment reviews in place.