

8 Component 2: Intergovernmental fiscal transfers to core government functions of eligible federal member states, interim and emerging administrations

Sub-component 2:1: Transfers to interim and emerging states for core government functions:

Results achieved:

Under this sub-component, the project started expanding services to Puntland State of Somalia and Jubbaland Administration of Somalia. First advance funds of U\$30,000 for each region have been released and remitted to both regions in Quarter III of 2015. In addition to advance, U\$26,094 of civil servant employees' salaries for Ministry of Finance (JSS) has been sent to Jubbaland through Central Bank of Somalia remittance mechanism via private banks that had been licensed by CBS. It is first fund from RCRF Phase II project that has gone to the regions since the effective date of the project.

Second payment from project fund for \$79,133 have been sent to Puntland State and it was successful step taken forward in building and strengthening relationship of Federal Government of Somalia with existing and emerging states of Somalia in sharing of project funds. In fourth quarter of 2015, two more payments to member states have been sent. The second payment brought total amount to states in \$251,240. Puntland has received \$151,810 While JSS got \$99,430.

Payment to existing Regional States in first quarter of 2016 totalled \$164,127.58. On the basis of Statements of expenditure submitted by States to project, \$111,822.32 has been sent over to Puntland State of Somalia where JSS has received \$52,305.26 as of March 31, 2016. In overall payment to Regional States, project has contributed \$415,367.58 of grant funds to those states as from the inception date of July 2, 2015 to March 31, 2016. In quarter (Q2 of 2016) Puntland received \$116,487.03 where Jubbaland State of Somalia got \$158,839.99 which brings total transfer to federal member states into \$275,327.02, thus total transfer to states from the inception to Dec 31, 2016 was \$690,694.60. Quarter starts from July 1 to Dec 31, 2016 Puntland and JSS received \$92,454.23 and 115,284.22 respectively. As of September 30, 2016, Puntland State received total transfer of \$472,573.58 where JSS got in the total of \$425,823.47. However, JSS and Puntland had received \$274,150.73 and \$412,215.16 respectively in quarter 4 of 2016 that brought total payment to member states into \$1,584,762.94 as of Dec 31, 2016. In quarter 1 of 2017, Puntland and Jubbaland have received \$189,851.82 and \$119,084.12 respectively. Total payment given to Puntland and JSS from the inception to March 31, 2017 was \$1,893,698.88.

Interim Galmudug Administration (IGA) and Interim South West Administration (ISWA) have also met the readiness criteria and first payment of advance of 50K has been disbursed to their respective bank accounts. As of March 31, 2017, Member States received \$1,993,698.88 of

project funds.

However, turning in of regional SOEs has little bit gone up in quarter II of 2017. Puntland, JSS, ISWA and Galmudug have received \$903,270.32, \$321,996.50, \$101,436 and \$144,700 respectively. Total payments to the states as of June 30, 2017 is \$3,465,101.70. In quarter III ending Sept 30, 2017, federal member states received \$874,743.12 that makes total payment to states \$4,339,844.82. However, benefitting Member States received in total \$2,140,869.13 in quarter 4 of 2017. In quarter I of 2018 JSS had received \$494,040 where SWSS and GSS had received \$66,167 and \$37,940 of project fund respectively. Teachers for Benadir Region started benefitting from project and in QI 2018 total payment in the amount of \$35,990 was paid to teachers.

Following discussions held with World Bank to further improve the fiscal transfer to the regions, a revised reimbursement cycle with cut-off dates was agreed between the government and World Bank. Given the large, and the increasing number of active funding streams, the workload in processing eligible costs is progressively increasing. Therefore, implementing a revised cycle will enable the project an adequate and predictable financing to governments, to guarantee sufficient liquidity.

To avoid missing an obligation already agreed with Federal Member States (FMs) based on timely fiscal transfer, the Project authorized funds transfer to three FMs via pass through process, namely, Puntland, Jubbaland and South West State of Somalia. **(If can add some more will be great)**

Challenges, Implementation Risks and Potential Mitigation Measures:

Implementation challenges in this component just include some procedural delays in transfer due to an existing payment process practice in the Ministry of Finance.

Sub-component 2:2: Intergovernmental fora on transfers and information exchanges:

Results achieved:

As the constitutional framework and analytical basis is developed, the project will support government to lay the foundations for a simple system of intergovernmental dialogue and associated resource transfers, to strengthen inter-governmental trust and, ultimately, of fiscal arrangement that promote greater equity in resource distribution among federal and sub-national governments. This will also finance technical assistance from FGS to support the interim and emerging states in inter-governmental relations.

To institutionalize the intergovernmental initiative the FGS has held the first workshop dialogue on Inter-governmental fiscal transfer arrangement in Mogadishu from October 31 2015 through November 4th 2015. During of the workshop, participants from existing and emerging states and Federal Government of Somalia had discussed key issues on revenue mobilization, profit sharing tax provisions and other various important topics. It had been through a constructive dialogue and debates on Socio-economic and future political framework for the country. The workshop was a follow up to a meeting held by the Ministers of Finance of the FGS and the regional member states during the launch of the Recurrent Cost and Reform Financing Project (RCRF II) facilitated by the World Bank in Nairobi in September 2015.

The then Minister of Finance of the FGS upheld a commitment he pledged during the launch of the RCRFII in Nairobi by calling regional member states to a meeting in Mogadishu aimed specifically for a discussion of an equal and justice distribution of national resources as well as initiating a process of knowledge transfer to the Regional Member States. Unequivocally, regional administrations responded the call and performed high-levels of participation to the meeting.

Given the fact that the Provisional Constitution of the Federal Republic of Somalia encourages some sort of dialogue on intergovernmental fiscal arrangement, the main theme for the meeting was just to start a process of political negotiation that covers issues of revenue sharing, negotiation on tax regimes, harmonization of customs and duties as well as fiscal transfers. Though such topics may not, in any way, be possible to be discussed in a single meeting, it was only considered this for a show of political will and consolidation commitments between the FGS and the member states regions. However, deliberations on fiscal arrangements would be an on-going negotiation from now on-words while this is considered as the milestone of the future negotiations.

It was widely agreed and noted that before a consensus can be obtained on a resource sharing formula and wider fiscal federalism issues, first it is necessary for all governments to enhance their financial Public Financial Management (PFM) systems and have a harmonized approach towards achieving such a goal. Therefore it was agreed that enhanced dialogue and cooperation between the FGS and regional member states will lead to a harmonized approach on PFM and fiscal arrangements that will in turn lead to solutions on the bigger issues such revenue sharing formulation. All delegates agreed that there was a clear and urgent need for continued discussions and as such the workshop was highlighted as one such initiative to facilitate this important dialogue. The workshop agreed on the creation of an inter-governmental committee for harmonizing tariffs and taxations across the country.

Mission of knowledge transfer to regions:

Following the formation of Finance Minister Forum in November 2015, several regional knowledge-sharing missions were undertaken. The mission secured to induce topics in reporting and preparation of financial statements. Wide spectrum of participants drawn from the Ministries of Health, Education, Finance, offices of the Accountant General, Auditor General and Regional Civil Service Commissions attended.

Knowledge sharing agendas included:

1. Ways and methods of tax collections;
2. Process of budget preparation;
3. Budget execution and payment process;
4. Rules and regulations of financial procedures;
5. Treasury management and expenditure;
6. Reporting and planning;
7. Procurement Process

Establishment of technical Intergovernmental Fiscal Federalism Committee:

Following the successful missions to the regions just to promote intergovernmental relations and to strengthen trust building between the FGS and FMS, a meeting was called by the Federal

Ministries Fiscal Federalism Forum (FMFF) to agree and to establish a technical committee that would support the FMFF stakeholders to discuss key fiscal policy issues that would promote the deepening of intergovernmental fiscal relations. Moreover, the technical committee would also provide recommendations to the FMFF on a fair and appropriate revenue sharing formula, expenditure and revenue assignments between the FGS and FMS. The work of the FMFF and the planned work of the technical committee are the first serious steps towards the goal of designing a workable intergovernmental fiscal framework.

Subsequently, technical representatives from the regional entities, FGS and World Bank representatives met in Nairobi between 12 to 15th of February 2017 to discuss and produce policy suggestions to the Ministerial Committee and to set up the structure of the intergovernmental technical committee. There after the committee elected Mr. Mohamed Kamil Yussuf, Permanent Secretary of Jubbaland Ministry of Finance, as Deputy Coordinator and five coordinating group members (one from each state). The committee agreed in their last meeting that the Federal Minister of Finance would nominate the Coordinator, who promptly nominated Mr. Jafer Ahmed, the DG of Revenue.

Recommendations provided by the IGFFC

Technical committees' first meeting produced policy suggestions relate to harmonize specific tax rates that include items of Khat, Cigarettes and departure tax. They recommended the following steps as a way to harmonize the rates.

- (a) Adopt of uniform specific tax of \$2.50 on Khat. This means states that currently don't impose tax on imported Khat will introduce this specific tax and the FGS will raise its specific tax from \$2 to \$2.5.
- b) A uniform rate will be applied to all brands of Khat regardless of differences in quality and the market prices.
- c) States will also explore ways to impose surcharge on top of this specific tax (as Puntland and FGS do) and share these revenues with the districts where ports of entry are located.
- d) Licensing of Khat Importers – ISWA, JSS and IGA to license Khat importers as the FGS and Puntland currently do. This will allow emerging states to encourage importers to use official borders crossing points instead of Al-Shabaab controlled areas. The Federal Government is encouraged to enter into an agreement with Kenyan government to ensure that only valid license holders are allowed to export Khat from Kenya to Somalia.
- e) States complained that Khat importers take the proceeds of their sale in cash. Usually, when a plane delivers Khat it also takes back bags full of cash of US dollars. Committee members felt that this is putting pressure on their currency market by lowering the amount of US dollars in circulation. The committee recognizes this is the work of the Central Bank of Somalia and recommends that Ministers of Finance encourage the CBS to develop strategies to deal, regulate and mitigate this problem.
- f) Only Puntland imposes international tariffs on goods coming from other parts of Somalia (Galmudug and Somaliland). To protect the Somalia's fragile common economic space states are encouraged not create inter-state trade barriers.

Eventually, on September 27th, 2017 Finance Ministers Fiscal Forum meeting attended by all regional finance ministers took place in Garowe, Puntaland to discuss, among other things, intergovernmental fiscal issues and to endorse recommendations put forward by the technical intergovernmental committee on tariffs and customs processes harmonization. After intensive deliberations the Finance Ministers' Forum endorsed committee's recommendation to harmonize the three proposed tariff rates which are detailed table below.

AGREEMENT ON HARMONIZATION RATES OF KHAT, CIGARETTES AND INTERNATIONAL DEPARTURE TAXES		
1.	Khat	Tax rate on \$2.5 per bundle
	License on khat importers	Federal Member States issue license of khat importers in their respective jurisdictions and FGS registers them
2.	Cigarettes	Tax rate on \$30 per cartoon
3.	International Departure	Tax rate on \$30 per international passenger
		Domestic travelers are exempted from departure tax

As was agreed in Garowe meeting, Finance Ministerial Forum again convened in Kismayo between December 16th to 20th to continue the discussion on harmonizing matters that affect an intergovernmental relation and with regard to the revenue management.

In line with Garowe agreement, the following items were discussed during the Kismayo conference:

- 1) Development of Committee's work Plan;
- 2) Discussion ways to harmonize sales taxes;
- 3) Review SOMA agreement;
- 4) Discuss and study revenue assignment
- 5) An additional agenda item adopted by the committee, which was an update of Surge Support Program and the sharing model of the initial \$6 million, proposed.

As an outcome, the forum agreed and finally endorsed the following points:

- I. Discussions on sales tax: after a thorough discussion, the committee agreed to review current federal sales tax act to reflect the realities of current federal system. The proposed draft of such well integrated and consultative law will be the Federal sales tax act to be adopted by all;

- II. SOMA agreement discussions. The forum agreed that Soma agreement had a lot of defects and is mainly contrary to
 - a- Geneva Convention
 - b- to the Somali sovereignty and nation hood. Specially from security perspective
 - c- to the tax law and
 - d. Somali parliament did not ratify it as the agreement of such magnitude needed to seek approval of Somali Federal parliament;
- III. Revenue Assignment - The forum having an in-depth discussion on the subject matter underscored that the subject matter cannot be discussed at this point of time unless all prevailing inland revenue taxes exercised by the FGS and FMS are harmonized. In this course, the forum identified 15 laws relate to inland revenue tax that need to be reviewed, modified and then harmonized;
- IV. The forum asked the technical committee to discuss ways to adopt ad valorem and report the options back to the Ministerial forum for consideration

The signed version of the agreement captured as a picture is as below with the original text

Challenges, Implementation Risks and Potential Mitigation Measures:

Challenges of this component include the following:

- De facto relation between the FGS and FMS;
- Ambiguity in the Provisional Constitution with reference to intergovernmental fiscal arrangement;

9 Component 3: Support of recurrent costs in health and education sectors in FGS and eligible member states, interim and emerging administrations

EDUCATION

Results achieved:

The project will support the FGS, Puntland and Jubbaland to expand their service delivery systems through improvement of accountability systems and support of recurrent costs in the education and health sectors. The specific activities include financing (i) establishment of basic accountability systems in both sectors (ii) Eligible salaries and allowances for teachers and health workers from 2015 to 2020 ; and (iii) eligible non-salary recurrent costs in the sectors.

Ministry of Finance has initiated engagement on health and education with Ministries of Health and Education in federal level to find accurate information on how to find easy way of service

deliverances to the public. Many of Non - Governmental Organization and other donors are operating in Education and Health sectors. Following various discussions between the leadership of the MoF and MoH on one side and numerous engagement by the project office on the side, a TOR was drafted by the project coordination office on the health sub-sector assessment which was also reviewed and validated by the leadership of the Ministry of Health before it is shared with Bank for approval.

On the education sector, assessment on financial standpoint was conducted by the World Bank, covering areas of planning and budgeting approaches, funding follow and banking arrangements, accounting and internal controls including payroll control and supporting system. On the bases of this assessment, the Bank agreed to finance salaries and allowances of teachers that are reflected in the appropriation act of 2017 both in FGS and Federal Member States, by providing qualifying numbers of teachers. Consequently, documentation of 1,258 teachers that has been preliminary reviewed by the Bank in FGS level and 1,195 teachers in Puntland were submitted. Puntland teachers financing was initiated from November 2016, while as of this reporting period, the Ministry of Education, Culture and Higher Education of FGS submitted all necessary documents relate to teachers' financing and up until now pending review with the World Bank.

In this reporting period, World Bank review on teachers' verification exercise completed, advisory report delivered spelling out findings observed and provided some recommendations as going forward. On the bases of this advisory report, the project was able to authorize three months salaries for 322 teachers operate in Banadir area through the FGS budget. In Puntland payment on teachers continued without hindrance.

Challenges, Implementation Risks and Potential Mitigation Measures

Even though, FGS has initiated engagement with health and education service deliverances where number of those institutions run of finance by private non-profit entities or NGOs. Main challenge is how to get accurate personal data for teachers and health workers. Dialogue and consultations among concerning ministries on data collection is ongoing and will be finalized soon in order to kick off service deliverances in federal level. Puntland State of Somalia has started paying teachers along with capturing full data on teachers.

Other worth mentioning challenges include:

1. No Comprehensive review of the education sector payroll system data reconciliation and integration of biometric functional capabilities to the sector workers' profile;
2. Sector's incapacity to respond quickly and to provide necessary information;
3. Delay in Verification mission postponed an earlier expectation of paying salaries;
4. Lack of Harmonization of salaries and incentives provided by the donors in the sector;
5. Sustainable financing approach is missing;
6. Time and attendance mechanism in school level;
7. Lack of clarity on the ownership of Public Schools. Definition of Public Schools need to be clarified

HEALTH

No worth reported activity was undertaken on this assignment except an agreement with World Bank to start operationalization of this sub component. In this regard, we have submitted an assessment ToR for the sector pending approval with the Bank.

10 Component 4: Project Management and Coordination

Overall update:

The component would support the coordination, administration, communication, management, procurement, monitoring and evaluation (M&E), as well as impact evaluation, auditing and dissemination of project activities in FGS, Puntland and the JSS. It would finance dedicated staff to cover administration, financial management, procurement and communication. It would also support efforts to develop and strengthen the Fiduciary Section of the offices of Accountant General in FGS, Puntland and JSS and interim and emerging states through the financing of equipment, furniture and filling, capacity building, technical assistance, and other inputs as required. The project supports the CBS with technical assistance to strengthen the payment systems and will also be the initial cost center for FY2015 and FY2016 external independent audit on all the Somalia MPF WB funded projects; the recruited audit firm would also support the offices of the respective Auditor Generals with technical assistance to provide annual audits

The project is under the supervision of the Ministry of Finance and other Ministries, Agencies and Departments (MDAs).

On the staffing side, five (5) Consultants to the EAFS plus the PFMRCU two (2) senior admin officers, along with a Deputy PFM Reform Coordinator who became RCRF II project manager has been recruited. Similarly, two Regional Program Managers have been recruited.

Auditors Opinion

III. FINANCIAL MANAGEMENT - (STATEMENT OF PROJECT MANAGEMENT'S RESPONSIBILITIES)

The Project Management is responsible to ascertain that the progress report and financial statements of the Project for the period ended March 31, 2018 are prepared, in all material respects, in accordance with the basis of preparation and accounting policies set out in Note 3 to the financial statements. In preparing these financial statements, the Project Management is required to select suitable accounting policies and then apply them consistently in conformity with Cash Basis International Public-Sector Accounting Standard (Cash Basis IPSAS) and the requirements of Financial and Accounting procedure of the State, 1961 as amended.

The Project Management is responsible for ensuring that proper accounting records are kept which enable the financial statements to be prepared in compliance with the basis of preparation and accounting policies set out in Note 3 to the financial statements as well as in accordance with the terms of the financing agreement for the Multi Partner Fund Grant Agreement Number TF0A0534 between the Federal Republic of Somalia and the International Development Association. The Project Management is also responsible for safeguarding the assets of the Project, and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Project Management assumes the responsibility to provide, and has provided, the Auditor General with all accounting records, supporting and other documents, minutes, and any other pertinent information and explanations, either orally or in writing, necessary for the audit.

Signed on behalf of the Project Management:

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Fatuma Osman Farah,
Accountant General

1. FUNDING SUMMERY

The Project implementation for this year is 12 months from 01 January 2018 to 31 December 2018, with an approved budget of US\$ 51,000,000 from 2015 to 2018 and commitment of the donors is as highlighted in the table below:

Source of funds	Donor Commitment	Amount received up to March 31, 2018	Undrawn balance up to Mar 31, 2018
	US\$	US\$	US\$
	(A)	(B)	(A)-(B)
Somalia Multi-Partner Fund (MPF) – World Bank	51,000,000	49,645,379.07	3,148,229.79
Total	51,000,000	49,645,379.07	1,354,620.93