This action is funded by the European Union

ANNEX I

of the Commission Implementing Decision on the financing of the Annual Action Programme in favour of Nepal for 2019

Action Document for Federalism Support in Nepal

| **ANNUAL PROGRAMME/MESuRE** | Federalism Support in Nepal  
  CRIS number: ACA/2019/040-787 financed under the Development Cooperation Instrument |
|-----------------------------|-------------------------------------------------------------------|
| **1. Title/basic act/CRIS number** | Nepal  
  The action shall be carried out at the following locations: in the 7 provinces and 753 local governments of Nepal |
| **2. Zone benefiting from the action/location** | Addendum No 1 to the Multiannual Indicative Programme between the European Union and Nepal for the period 2014-2020¹ |
| **3. Programming document** |  
  Sector 3 of MIP (2014-2020): Strengthening democracy and decentralisation  
  DEV. Assistance: YES² |
| **4. SDGs** | Main SDG: 16 on Peace and Strong Institutions,  
  Other significant SDG: 17 on Partnerships and 5 on Gender Equality |
| **5. Sector of intervention/thematic area** | Total estimated cost: EUR 32 350 000 |

¹ C(2018)4741 of 20 July 2018  
² Official Development Assistance is administered with the promotion of the economic development and welfare of developing countries as its main objective.
Total amount of EU budget contribution EUR 32 350 000 of which
- EUR 28 000 000 for budget support
- EUR 4 350 000 for complementary support

<table>
<thead>
<tr>
<th>7. Aid modalities and implementation modalities</th>
<th>Budget Support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct management through:</td>
<td></td>
</tr>
<tr>
<td>- Budget Support: Sector Reform Performance Contract</td>
<td></td>
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<tr>
<td>- Procurement</td>
<td></td>
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<tr>
<td>- <strong>Indirect Management</strong> with the World Bank (WB)</td>
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<tr>
<td>- <strong>Indirect management</strong> with the entity to be selected in accordance with the criteria set out in section 5.4.1</td>
<td></td>
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</table>

| 8 a) DAC code | 15112 Decentralization and support to infra-national administration |
| b) Main Delivery Channels | 12000 Recipient Government, International Organisation to be defined |

<table>
<thead>
<tr>
<th>9. Markers (from CRIS DAC form)²</th>
<th>General policy objective</th>
<th>Not targeted</th>
<th>Significant objective</th>
<th>Principal objective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Participation development/good governance</td>
<td>☐</td>
<td>☐</td>
<td>X</td>
<td></td>
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<tr>
<td>Aid to environment</td>
<td>X</td>
<td>☐</td>
<td>☐</td>
<td></td>
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<tr>
<td>Gender equality and Women’s and Girl’s Empowerment</td>
<td>☐</td>
<td>X</td>
<td>☐</td>
<td></td>
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<tr>
<td>Trade Development</td>
<td>X</td>
<td>☐</td>
<td>☐</td>
<td></td>
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<tr>
<td>Reproductive, Maternal, New born and child health</td>
<td>X</td>
<td>☐</td>
<td>☐</td>
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</tr>
</tbody>
</table>

| 10. Global Public Goods and Challenges (GPGC) thematic flagships | N/A |

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² [http://www.oecd.org/dac/stats/annex2.htm](http://www.oecd.org/dac/stats/annex2.htm)
Nepal adopted a new Constitution in September 2015, with the intent to transform the country from a centralised unitary state into a federal state. The Constitution stipulates three tiers of government: one Federal government, seven Provincial governments, and 753 Local governments (municipalities and rural municipalities). Basic devolution of power is guaranteed to the various levels of governments, through exclusive and concurrent powers and responsibilities.

The EU will support the government of Nepal in this massive reform of the State for a period of 4.5 years, in a two-ways approach: 1) by focusing on strengthening the capacities of the provincial and local governments, so that they can fulfil their mandate and functions as enshrined in the Constitution, and 2) by focusing on improving fiscal decentralisation to give provincial and local governments the means to operate. The EU’s total contribution will be of EUR 32.35 million from sector 3 of the Multi-annual Indicative Programme (MIP) 2014-2020.

1) The EU will support the joint donor-Government Provincial and Local Governance Support Programme (PLGSP), which covers the years 2019-2023, through sector budget support (Sector performance reform contract) for a total amount of EUR 28 million. This programme aims to strengthen the capacities of elected representatives and the public administration, in order to create functional, sustainable, inclusive and accountable provincial and local governments. The PLGSP will be led and administered by the Ministry of Federal Affairs and General Administration (MOFAGA) and co-funded by the UK Department for International Development (DFID), Switzerland and Norway. In addition, the EU’s support entails EUR 2 million as complementary measures for the technical assistance service provider (TASP) to the PLGSP, providing technical support to provincial and local governments.

2) The EU will also support the Integrated Public Finance Management Reform Project (IPFMRP), as initiated by the Multi-Donors Trust Fund (MDTF) administered by the World Bank (WB), with an amount of EUR 2 million through complementary measures. This action entails strengthening the effectiveness of selected public finance management institutions and related procurement, systems and procedures at the three different levels of governments.

1. CONTEXT ANALYSIS

1.1 Context Description

Nepal is a Least Developed Countries (LDC) situated between China and India. It is the 16th poorest country in the world and the 2nd poorest in Asia (after Afghanistan) in terms of per capita income (World Bank 2018). The country is ranked 148th in the world in the Human Development Index (UNDP 2018). GDP per capita has increased and is expected to reach USD 1,143 in 2019. The poverty rate has steadily decreased over the years, it varies across the country, being particularly high in rural areas and lower in urban areas. In most parts of the country, economic opportunities are limited, as a result, migration, in particular of youth, has dramatically increased in the recent years.

Nepal is an EU like-minded partner for climate action as the Himalayan mountain range has a profound effect on the climate of the South-Asian region. It is also important to note that Nepal is one of the most disaster-prone countries in the world. The devastating earthquakes in 2015 were followed by trade disruptions leading to a fuel crisis, which impacted the entire economy. In addition, the heavy monsoon rains sweeping across South Asia in 2017 affected 1.1 million of the Nepalese population.
In accordance with its geographical diversity, Nepal is also extremely diverse in terms of ethnicity, languages, cultures and religions. Indigenous peoples comprise 35.8 percent of the total population, while Nepal has legally recognized 59 indigenous nationalities, referred to as Adivasi Janajati. While today the country wishes to embrace its diversity, gender and social disparities are still prevalent. For example, the National Living Standard Survey (NLSS) 2011 found that 40% of women in Nepal were illiterate, in comparison to only 14% of men, and that 60% of Terai women were illiterate compared to 32% of women in the hills and mountains.

Nepal has gone through major political changes, transition and transformation for the last three decades. Major milestones of such changes include: popular movement and restoration of multi-party democratic system (1990), the signature of the Comprehensive peace accord (2006) putting an end to the armed conflict (1996-2006), political transition and promulgation of a constitution, introducing a federal system of governance (2015).

The constitution officially institutionalized Nepal as a federal democratic republic with three tiers of governments based on the principles of coexistence, collaboration and coordination, with clear mandate to address the inequalities and discriminations. In addition to the federal government, 7 provincial and 753 local level governments have been formed with the powers, functions and responsibilities of the state divided among them.

Besides the constitution, which clearly envisions Nepal as an inclusive state and guarantees the right to equality for all its citizens, Nepal is also a signatory to various international conventions, among others CEDAW, ILO Convention 169 on the Rights of indigenous peoples and therefore legally committed to gender equality and social inclusion. Accordingly, the government of Nepal’s (GoN) gender equality and social inclusion (GESI) policies and guidelines have been adopted as of 2017 in seven sectors. While implementation of those policies is slow and weak, strides forward have been made. For example in 2014, only 10.6% of the civil servants were women, while following the 2017/18 elections, women now hold 40.79% of political positions in the country, which is unprecedented in Nepal’s political history and also admirable in the global context. In particular at the local level, a total of 14,349 women now represent local constituencies.

High socio-economic growth, including job creation, and bringing down poverty from 23% to less than 5% of the population, is a top priority for the Nepal's new government. Federalism is seen as a means of achieving inclusiveness by bringing governance closer to the citizens and of realizing the desired socio-economic growth through effective service delivery. Therefore, the effective implementation of federalism at this point in time represents a key opportunity for Nepal's sustainable development.

1.2  Policy Framework (Global, EU)

The EU Federalism support is a key intervention of the Addendum n°1 to the MIP 2014-2020, which confirmed sector 3 “Strengthening democracy and decentralization”. It is consistent with the principles and spirit of the EU Global Strategy 2016, especially with the priorities related to ‘State and Societal Resilience’, and ‘Global Governance for the 21st Century’. It is also in line with the integrated approach to conflict and crisis, the 2017 Joint communications on resilience, the Gender Action Plan (GAP) II, the Council conclusions 2017 on indigenous peoples.
Support to decentralisation through budget support is fully in line with the 2013 Commission Communication “Empowering local authorities in partner countries for enhanced governance and more effective development outcomes”\(^3\).

The Commission Communication "The future approach to EU budget support to third countries"\(^4\) highlighted already the need to strengthen the capacity of local authorities to act as an essential component for the state domestic accountability system, thus contributing to enhance government's capacity to deliver services to final beneficiaries.

The budget support has been designed in conformity with the 2016 EU methodological note on "providing EU budget support in decentralised contexts".

It will contribute across all SDGs with more relevant impact on SDGs 5 (Gender equality), 16 (Peace and strong institutions) and 17 (Partnerships). Furthermore, this prospective support is aligned to the priorities 'Peace', ‘Prosperity’ and ‘Partnerships’ of the EU Consensus on development and notably focuses on democracy, effective and accountable institutions and the rule of law.

1.3 Public Policy Analysis of the partner country/region

The 2015 Constitution describes the new structure of the state mainly in its section 5: Structure of the state and division of state powers and annexes 5, 6, 7, 8 and 9 (exclusive and concurrent powers of federal, provincial and local level). In addition several acts or laws have been enacted to facilitate the implementation of the reform: Local Governance Operation Act 2017, National Natural Resources and Fiscal Commission Act 2017, Inter-Governmental Fiscal Management Act 2017, Staff Adjustment Act 2017.

The implementation of the Federalism reform will be mainly done through the Provincial and Local Governance Support Programme (PLGSP). This is a national sectoral programme from the Government that spans 2019-2023, and is co-funded by development. The cost of PLGSP is estimated at EUR 100 million with a contribution of about EUR 27 million from the government of Nepal and EUR 73 million from Development partners\(^3\). The programme will provide an overarching framework to all sub-national governance programmes in Nepal. The programme will be led and administered by the Ministry of Federal Affairs and General Administration.

As the most recent and crucial step in the transition process, the new federal government has prepared the first full federal budget in financial year (FY) 2018/2019, with separate Grants book for provincial and local governments, as per the provisions of the constitution and the intergovernmental Fiscal management Act, 2017. Similarly, both the provincial and the local governments have enacted their first full year budget to be financed by both fiscal transfers from the federal budget and from their own resources.

Given the limited revenue bases assigned to provincial and local governments (PLGs), and their weak revenue generation and administration capacity, the resultant gaps at the PLGs will have to be met primarily through fiscal transfers by the central government. There is an apprehension that high

\(^3\) COM(2013)280

\(^4\) COM(2011)638

\(^3\) The donors to PLGSP are DFID (EUR 23.45 million), Norwegian Embassy (EUR 17.55 million), Switzerland cooperation (EUR 1.75 million) and EU (EUR 30 million).
fiscal dependence on the central government will adversely affect the quality of devolution and autonomy of PLGs.

Three acts endorsed by the Parliament provide the legal framework for revenue mobilization in Nepal: (i) Local governance operations Act 2017, which outlines the financial jurisdiction of local governments and defines the distribution of authority for policy formulation, determination of tax rate, and collection of taxes; (ii) National Natural Resources and Fiscal Commission (NNRFC) Act 2017 to manage the inter-governmental fiscal transfers to address vertical and horizontal imbalances between federal and PLGs and (iii) Inter-governmental Fiscal Management (IGFM) Act 2017, which specifies sharing of PLGs in VAT, domestic excise duty, and royalties.

EU Federalism support contributes to address some major challenges in the implementation of the federalism process, namely: inter-governmental coordination and implementation, sub-national government systems and procedures, institutional capacity of sub-national governments, empowerment of elected officials and capacity development of provincial and local level government staff, ensuring accountability of local governments to the citizens at the grass-root level as well as strengthening the public finance management systems to reinforce accountability in the use of resources.

The support is aligned to the public policies and legal frameworks of the GoN, and consistent with Nepal’s overall long-term goal of ‘Prosperous Nepal, happy Nepali’ and more specifically its priorities under Envisioning Nepal 2030, whereby the government of Nepal seeks to achieve all the Sustainable Development Goals (SDGs) and become an inclusive, equitable, and prosperous middle-income country by 2030.

1.4 Stakeholder analysis

Government of Nepal

Supporting Federalism in Nepal involves collaboration with the governments, ministries and public agencies at all three levels. Key stakeholders and their roles in federalism include:

Federal Level:

Ministry of Finance (MoF): foreign aid policy formulation and execution, foreign aid coordination, development cooperation agreements with development partners, federal fiscal policies, federal budget preparation, inter-governmental fiscal transfers and management, and public finance management (PFM). The main functions of the MoF in relation to the fiscal federalism are coordination among the federal and PLGs agencies, drafting of fiscal laws and regulations, and preparing necessary criteria and basics for the implementation of Inter-Governmental Fiscal Management (IGFM) Act.

Ministry of Federal Affairs and General Administration (MoFAGA): coordination of federalization of the governance and public administration, deployment and adjustments of civil servants, development of model acts and laws required by the three levels of governments. MoFAGA is mandated for coordination, facilitation, and institutional development support to local governments. It also fosters inclusive development by promoting peoples’ participation in local governance.

National Natural Resource and Fiscal Commission (NNRFC): NNRFC is one of the key actors in federalism implementation with roles in policies and strategies for sharing natural and fiscal resources among the governments. The NNRFC is responsible for determining respective shares of revenue among the federal government and sub-national governments.
Office of the Auditor General (OAG): key stakeholder in ensuring financial accountability through external audits at all three levels of government, PFM related roles, management of fiduciary risks, capacity development of accounting and auditing system at sub-national level.

Financial Comptroller General’s Office (FCGO): GoN’s PFM responsibilities, management of fiduciary risks, treasury control and management.

National Planning Commission (NPC): is headed by the Prime minister and is the advisory body of the GoN for formulating a national vision, periodic plans and policies for development. It assesses resource needs, identifies sources of funding, and allocates budget for socio-economic development. It serves as a central agency for monitoring and evaluating development plans, policies and programs.

Provincial Level:

Office of the Chief Minister and Council of Ministers (OCMCM): overall responsible for the exclusive and concurrent powers of the state provisioned in the schedule 7 and 8 of the constitution, respectively. It is the newest state structure in the federal governance system. PLGSP steering and coordination role is assigned to the provincial governments in all 7 provinces.

Sector ministries (provincial level): 7 ministries with key role in sector coordination. New institutional set-up, many structural, procedural and systemic supports are needed to enhance their effectiveness.

Province Treasury Comptroller's Office (PTCOs) – new PFM agency at provincial level, provincial treasury/fiscal management and control.

Provincial Centre for Good Governance (PCGG): restructured offices of Local Development Training Academy (LDTA) in each province, key role in PLGSP for capacity development of sub-national governments (staff and elected representatives).

Local Level:

Local level governments: closest to the communities, democratic representation, inclusive governance and service delivery (including the sector results), the 753 municipalities are the key stakeholders in making federalism a success. Support to federalism will contribute to strengthening of decentralised public administration, fiscal decentralisation and capacities of the elected officials and staff at the local levels.

Private Sector and Civil Society Organizations (CSO)

Private Sector:

Complementarities and contributions of private sector organizations in delivery of sector results and services by the government are important and crucial for achieving Nepal’s development goals. In the context of federalism support, the private sector organizations (research and training institutions, consulting firms, etc.) will provide capacity development and Technical Assistance (TA) services to the governments at all levels. Furthermore, they will be the major driver of economic growth at province level and should play a central role in service delivery in sectors like tourism, urban and peri-urban transportation, and waste management.

Civil Society Organisations (CSOs) and Non-Governmental Organisations (NGOs):

CSOs play a key role in mobilizing and representing voices of people, especially the poor, women, indigenous peoples, Dalits and other traditionally excluded groups, which is an equally important contribution towards the fulfilment of the commitments of the GoN for inclusive development
through ensuring civic participation in all spheres of public engagement. PLGSP has considered the role of CSOs as one of the important components in its results framework (through promotion of community engagements and public accountability). Furthermore, CSO could also play an important role in social service delivery at local level, including in remote areas.

1.5 Problem analysis/priority areas for support

1.5.1 Problem analysis

The Constitution of Nepal 2015 provides a historic opportunity in promoting inclusive development and democratic accountability through provisions for institution building and deepening of good governance practices and reforms at the federal, provincial and local levels. Despite such strong constitutional and legal framework, there are challenges that cut across the different dimensions of the federalism, including inclusive governance, public administration, fiscal decentralisation, PFM and service delivery. The main challenges identified under PLGSP are:

- **Insufficient inter-governmental coordination and relationships:** Necessary enabling legislation, structures and systems and capacities at federal, provincial and local government entities are yet to be created for a working inter-governmental relationship based on the principles of co-existence, cooperation and coordination.

- **Limited systems and procedures for strong sub-national governments:** The systems and procedures for effective governance at provincial and local level are yet to be fully established. The provincial and local governments are in need for appropriate legislative, regulatory and administrative guidance from federal level to effectively operate as whole of the government entities.

- **Weak institutional capacity at sub-national level:** Provincial and local governments need to improve technical skills of their human resources to cope with the new governance and administrative context, and change of mind-set. This weak capacity at subnational level is likely to constrain the management of public funds at the local level, and thus have an immediate negative impact on service delivery. Similarly, the local elected officials require support in empowering them to perform their constitutional functions as defined in the 2017 Local Governance Operational Act (LGOA). In these contexts, the provincial and local level governments require sustained and intense institutional capacity development support.

- **No established PFM processes yet for intergovernmental or subnational-level PFM activities:** This lack of systems, processes, and capacity at the subnational level is likely to pose an immediate risk to the use and management of resources. Block grants are quarterly released from federal level to the bank accounts of the concerned provincial or local level, which will further delegate to spending units according to their own system. In addition, for their budget, they may have their own source of revenue that they can manage themselves with their own annual plan and programme.

- **Low level of community participation and accountability:** the link between citizens and their newly elected local governments for meaningful participation and accountability is the backbone for success of the federal system of governance. In the absence of adequate federal or provincial legislation, guidelines and institutional capacities, local governments cannot perform their constitutional function as responsive and accountable governments.
1.5.2 Priority areas for support

The EU support to federalism will focus on:

- **Supporting Government of Nepal for federal devolution:** Commitment to the federal devolution of state powers as provided in the schedules of the constitution and the legislation enacted for the purpose by Parliament will be emphasized. Needs based capacity development support to the staff and elected representatives;

- **Supporting GoN’s efforts for ensuring transparency and accountability in sub-national governance:** the EU Federalism support will promote transparency in the governance process, i.e., decision-making, formulation and implementation of plans, programme and budget, coordination between all agencies;

- **Supporting local governments in improving service delivery** in all sectors and notably in other sectors already supported by EU (agriculture, education, nutrition).

- **Ensuring complementarity of interventions with the other EU cooperation and development supports**;

- **Supporting local governments in improving service delivery** in all sectors and notably in other sectors already supported by EU (agriculture, education, nutrition).

- **Strengthening the effectiveness of selected PFM institutions and procurement institutions, systems, and procedures at the federal and subnational levels.** Ongoing and additional support to the PFM reform through the Multi-Donor Trust Fund (MDTF) is expected to improve fiduciary risk management;

- **Supporting public institutions at all level for mainstreaming gender equality and social inclusion (GESI):** PLGSP will support Nepal’s public institutions for mainstreaming GESI by improving governance systems, procedures, planning, execution, monitoring and evaluation of development interventions;

- **Supporting financing local initiatives through the innovative partnership fund where local authorities will implement project related to local investments.**

1.6 Other areas of assessment

1.6.1 Fundamental values

Nepal is a young democracy still consolidating the comprehensive peace accord of 2006. It has ratified many of the key international human rights instruments and abolished the death penalty. Citizens are more able to exercise their political freedom and political will as well as economic rights than a decade ago, but little progress has been achieved in enhancing accountability over the provision of state services and public goods notably at the local level.

The 2015 Constitution guarantees key fundamental rights, including freedom of press, opinion and expression, as well as the right to food and right to information. However, further enhanced implementation capacity is key for the full realisation of these rights.

Although Nepal has independent rule of law institutions, they are underperforming notably due to a lack of sufficient resources. Case backlogs and enforcement of court decisions remain critical issues.

Issues of caste-related, ethnic and gender discriminations related to the country's culture and traditions still exist, though much has been done to reduce their impact, including through EU funded activities, for instance through the European Instrument for Democracy and Human Rights (EIDHR). In rural areas, the practice of bonded labour has been abolished, but the people previously in this situation still struggle to make a living and have a very weak social and economic position.
Gender inequalities associated with land tenure persist and much remains to be done to tackle traditional practices which may continue to disadvantage women who may not be aware or able to effectively claim for their legal rights.

The government of Nepal struggle to operationalise the rights-based approach. Although there is a Right to Information (RTI) Act, to date CSOs do not appear to have been important drivers of the ‘demand’ for information and the opportunities to enhance social accountability remain somewhat restricted. More broadly, civil society itself suffers from lack of effective coordination, a weak financial base, limited capacity and low levels of political visibility.

1.6.2 Macroeconomic policy

Nepal’s economy has been rebounding since the 2015 earthquakes, with economic growth reaching 7.9% in FY 2016/17 and 6.3% in FY 2017/18, supported by political stability, more reliable electricity supply, construction, record tourist arrivals, rising private consumption and government spending. Inflation has remained low throughout 2018, at 3.9% in September 2018 (y/y). The risks are broadly linked to the rising fiscal deficit, which reached 6.5% of GDP in FY 2017/18, and widening current account deficit, which reached 8.2% of GDP.

The authorities pursued in 2017/18 their domestic revenue mobilisation efforts, with tax revenue rising to 21.9% of GDP from 21.0% of GDP in FY 2016/17. This however was not sufficient to compensate for an extraordinary surge on the expenditure side, with total expenditures soaring to 32.0% of GDP from 27.5% in the previous year. The fiscal deficit thus rose to 6.5% of GDP, from 3.1% in 2016/17, with public debt ratios deteriorating by 4 points of GDP and official reserves falling from 8.3 to 7.2 months of imports.

On the expenditure side the government reckons that expenditures related to federalisation will need to increase by 2.2 points of GDP in FY2018/19, with revenue-sharing from federal to subnational level kicking-in at 4.6% of GDP. The deficit is oriented towards 5.0% of GDP, while public debt should continue rising to 33.1% of GDP (still in the Debt Sustainability Assessment (DSA) low risk bracket) and official reserves deplete further to 5.7 months of imports. On the face of such an expansionary fiscal policy, the IMF warns in its recent Article IV consultations that fiscal expansion exceeds the economy’s aggregate absorptive capacity and is not well anchored in a realistic Medium Term Expenditure Framework (MTEF) to ensure quality and fiscal and external sustainability.

The WB Nepal development update of November 2018 recommends the GoN to more closely engage with the private sector as financing needs far surpass available public resources and available donor funding. It also stresses the importance of implementing PFM reforms such as public investment management to improve capital budget execution, and establishing proper PFM systems at the subnational level to seize on the transformational opportunities of implementing federalism and crowd in private investment.

1.6.3 Public Financial Management (PFM)

Key progress achieved so far in implementing PFM reforms include: (i) drafting and submission to Parliament of key pieces of legislation (Financial procedures and Fiscal responsibility Act, Audit Act, Public procurement Act); (ii) enhancing the institutional framework for fiscal decentralisation (nomination of a head for the National Natural Resources and Fiscal Commission (NNRFC), activation of the Intergovernmental fiscal council, deployment of accountants in all new local governments, gradual rollout of the Sub-national Treasury Regulatory Application (SuTRA) Information Technology (IT) system for budgeting, accounting and reporting of local governments, establishment of provincial treasuries and confirmation of District treasuries; (iii) enhanced budget transparency (publication of the MTEF, publication of whole-of government financial statements for
FY2017/18, improved oversight by the Public accounts committee); (iv) strategizing towards integration of IT financial management systems; (v) ensuring strong revenue mobilisation through sustained tax policy and tax administration reforms.

Local revenue mobilisation will be challenging, as it is expected to add 1.2 point of GDP to tax revenue ratios. Indeed, in line with the Local governance operation Act, subnational governments also have locally shared revenues. Registration fees for houses and land, advertisement tax, vehicle tax and entertainment tax are shared rights of the provinces and local units. Service fee, registration fee, fine, tourism fee and royalty received from natural resources are concurrent powers of the federal, provincial and local units. In case of shared jurisdiction, the province keeps 60% of the taxes it collects and transfers 40% to the local divisible fund. Likewise, when the local level collects taxes, it keeps 60 percent and transfers 40 percent to the provincial consolidated fund. The funds are divided among the different units based on the formula set by the NNRFC.

1.6.4 Transparency and oversight of the budget

The main reference documents for budget transparency and oversight include the following: Budget speech 2018/19, Executive budget proposal 2018/19, Enacted budget 2018/19 (Red book) of the Federal level, Mid-year budget execution report, Audit report for fiscal year 2016/17.

Until 2015, Nepal's Open Budget Index (OBI) scores had been consistently stable, showing little variation from one survey to another. In 2015 however, Nepal’s score abruptly fell from 44/100 to 24/100, reflecting more a change in OBI methodology to give higher scoring value to public participation, rather than deterioration in budget transparency as such. In the OBI survey 2017, Nepal’s score rose substantially to 52/100. Six of eight key budget documents are now available to the public in a timeframe consistent with international standards, as opposed to five only in the OBI 2015, and the Executive’s budget proposal is now published in a timely manner.

Overall, the authorities have continued to show their commitment to budget transparency, as demonstrated by a surge in Nepal’s OBI score in 2017. The Executive’s budget proposal and the Enacted budget are made available to the public in a fashion that meets international standards. Quality and comprehensiveness of the information included in the budget documents has started to improve and quarterly federal budget execution reports are published.

Concerning budget oversight, the mandate and resources of the OAG have been widened to allow for enhanced coverage of subnational governments. Finally, the parliamentary Public accounts committee has started to scrutinize federal government’s agencies more closely in 2018.
2. **Risks and Assumptions**

<table>
<thead>
<tr>
<th>Risks</th>
<th>Descriptions</th>
<th>Risk level H/M/L</th>
<th>Mitigation Measures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Decline in continuous political support for the federalisation process</td>
<td>Political and governance transition for effective implementation of federalism may not be fully materialized</td>
<td>L</td>
<td>Support in strengthening public institutions at all government levels and reinforcement of the policy dialogue</td>
</tr>
<tr>
<td>Weak sector strategies and policies and lack of involvement of sectoral ministries at federal level</td>
<td>Uncertainties with sector priorities and implementation of activities are anticipated, with the reorganization of line ministries and ongoing revisions of the functions and staffing at federal and provincial level</td>
<td>L</td>
<td>Together with federalism support, the DPs need to proactively support the governments and sectoral agencies as per need in updating/implementing sector policies and priorities. Effective services and sector results are core of the success of federalism. Coordination mechanisms will have to be set at federal level between MOFAGA and sectoral ministries</td>
</tr>
<tr>
<td>Increasing corruption and fiduciary risks</td>
<td>Financial mismanagement and corruptions are likely to increase especially in the early years of federalism</td>
<td>H</td>
<td>Incorporate third-party monitoring and encourage citizen engagement for public accountability. Harmonize fiduciary risk mitigation measures with other DPs and federal agencies of the government such as the Financial Comptroller General Office and the Office of the Auditor General</td>
</tr>
<tr>
<td>Conflict stemming from marginalized groups, such as indigenous peoples and other minorities</td>
<td>Protests might arise if citizen's rights are not fully considered by provincial and local governments, and land issues are not addressed</td>
<td>L</td>
<td>Citizen's engagement, inclusive participation and accountability measures are foreseen in the programme notably in its outputs 9, 10, 11. Respect for the right to free, prior and informed consent should be promoted as UN Declaration on the rights of indigenous people (UNDRIP), ILO Convention 169 and EU commitments under CC on indigenous peoples 2017</td>
</tr>
<tr>
<td>Newly elected female leaders fail to fulfil their roles and responsibilities and these opportunities to lead and participate will be taken away in the next round of elections.</td>
<td>Research shows that beneath a layer of institutional formality, there are built-in limits to women achieving the capabilities required to perform their roles</td>
<td>H</td>
<td>Reinforcing capacities of newly elected female leader paying attention to their special needs and functions through specific trainings delivered by the PCGG on GESI related matters</td>
</tr>
<tr>
<td>Natural disasters</td>
<td>Disruption of services might occur if disaster risk management is not fully operational</td>
<td>M</td>
<td>By increasing the capacity of the public administration, this programme under outputs 13 and 14 includes disaster risk management support at sub-national government level</td>
</tr>
</tbody>
</table>

3. Lessons learnt and complementarity

3.1 Lessons learnt

The EU has gained experience from its previous support in governance, notably the Nepal Peace Trust Fund, the Electoral support programme and its current involvement in the MDTF for PFM reform support. Strong government leadership for the programme (through clearly assigned execution role to one of its central agencies), good coordination among DPs and a rigorous monitoring, throughout the program cycle are key factors for success of externally financed policy support as well as framework program interventions.

3.2 Complementarity, synergy and donor coordination

EU will continue to be an active member of the International Development Partner Group (IDPG) on Federalism support for sharing and exchange of information, work collectively on issues of common interest, and coordinate activities for the federalism support initiatives (with focus on sub-national level). Most of the DPs have adapted and aligned their country support strategies and frameworks to
the new context of Nepal. Strengthening the new federal institutions, supporting setting up systems and procedures, and developing capacities of the human resources have been common key features in the development cooperation strategies of the DPs.

The EU Federalism support will complement other DPs programmes in support to local governance (USAID, GIZ, Australian Embassy). Notably, it will complement the EUR 4.6 million capacity development support to governance programme (2019-2022) from GIZ which seeks to support PLGSP in three key areas: inclusive planning and decision-making, service delivery and capacity development institutions and practices.

On fiscal decentralisation, EU will increase its active involvement in the MDTF (2017-2022) for PFM reform led and administered by the World Bank and jointly funded by other donors: Norwegian, Danish, Australian, and Swiss embassies as well as DFID and USAID.

It will also complement its previous support to the Asian Development Bank (ADB) in which EU contributed up to 2017 to the financing of the Strengthening Public Management Program (SPMP) for the development of a Municipal Administration Revenue System (MARS).

4. DESCRIPTION OF THE ACTION

4.1 Overall objective, specific objectives, expected outputs and indicative activities

The EU Federalism support has adopted a two-way approach, on capacity building of people and institutions through the PLGSP and on fiscal decentralization through the Integrated Public Finance Management Reform Programme (IPFMRP).

I) Support to PLGSP:

The overall objective (impact) of the Action is to support the PLGSP for the creation of functional, sustainable, inclusive and accountable provincial and local governments.

The program aims to reach 3 specific objectives (outcomes):
1) Government institutions and intergovernmental mechanism at all level are fully functioning in support of federal governance, as per the constitution,
2) Provincial and local governments (PLGs) have efficient, effective, inclusive and accountable institutions, and promote innovations and partnership for inclusive local development
3) Elected representatives and civil servants at provincial and local governments have the capacity and serve citizens to their satisfaction.

The induced outputs are:
1A) Federal ministries and agencies are supporting the PLGs in policy and institutional spheres for implementing federal governance;
1B) Inter-governmental administrative mechanisms are fully functional;
2A) Provincial governments have functional, inclusive and accountable institutions;
2B) Local governments have functional, sustainable, inclusive and accountable institutions;
2C) Provincial and local governments promote innovations and partnership for inclusive governance and local development;
3A) Elected representatives and civil servants of provincial governments are capaciticated to serve citizens to their satisfaction;
3B) Citizens are satisfied from the services of the capaciticated elected representatives and civil servants of local governments.
The 14 direct outputs are:
1) Federal level institutions develop legislations and policies to support provincial and local governments;
2) Federal level institutions develop tools and systems to support provincial and local governments in a consultative process;
3) Inter-governmental administrative mechanisms strengthened and functional,
4) Provincial governments drafted legislation
5) Modernized provincial government systems enable horizontal and vertical accountability to all citizens and mainstream GESI;
6) Provincial governments manage core public administration functions,
7) PCGGs made operational to deliver capacity development services 8) Modernised local governments have strong administrative system, accountable and public financial management system;
9) Local government systems enabled horizontal and vertical accountability to all citizens,
10) Local governments systems mainstream GESI in their service delivery;
11) Local governments systems enable citizen engagement and inclusive participation,
12) Innovation and partnership fund is operational and transparently supporting local governments innovative practices;
13) Elected representatives and civil servants at the province level are incentivized and trained for delivering high quality services;
14) Local governments' elected representatives and civil servants are empowered and trained for delivering high quality services.

Budget Support
The main indicative activities to implement the budget support package are policy dialogue, financial transfers, capacity development and monitoring performance. In particular:
- Continued policy dialogue with the government, focusing on results, disbursement conditions of the Sector Reform Performance Contract (SRPC) and adequate implementation of complementary support;
- Regular monitoring with respect to macro-economic and PFM, as well as budget transparency;
- Preparation of the disbursement files and monitoring of performance targets and indicators to be used for disbursement;
- Participation as appropriate in federal and provincial level coordination mechanisms, sector meetings / reviews and technical working groups.

There will be two complementary support components:

1) Support to PLGSP - including the following indicative activities: capacity building and provision of the technical experts and support staffs to the programme implementation unit; strengthen, monitoring and support reporting common results framework and indicators; training for participatory policy formulation, coordination for all three levels of government, improved service delivery, etc.
2) Integrated Public Finance Management Reform Programme (IPFMRP)

The IPFMRP supported by the MDTF, provides a sound strategic framework for supporting implementation of federalism with focus on sub-national levels of government. The IPFMRP indicative list of activities foresees building and provision of technical expertise and support staffs for implementation of National PFM reform plan (2016-2025) at local and provincial level. Training and awareness raising aimed at: (i) better capital budget execution and revenue administration, (ii) enhanced professional capacity of key PFM stakeholders and (iii) enhanced PFM accountability through strengthened audit function.

4.2 Intervention logic

EU foresees to contribute to PLGSP through budget support with a contribution of EUR 28 000 000. PLGSP combines programmatic components of formulation and execution of policies and strategies (related to restructuring and redefining public administration and fiscal decentralization), contributing to institution building at all levels, and towards capacity development of the human resources, systems and procedures for institutionalizing the governance and accountability among the three-levels of governments.

An amount of EUR 4 000 000 will be left for complementary support, including a contribution to the Multi Donor Trust Fund on the PFM aspect of fiscal decentralisation. The EU support to the MDTF aims at strengthening the effectiveness of selected PFM institutions and related procurement, systems and procedures at the federal and subnational levels.

The budget support aid modality is justified by the national scope of the PLGSP and its government-led management structure. It provides effective leverage for policy reforms and promote policy dialogue. Acting as a major financial contributor to the PLGSP, EU will have a considerable policy dialogue leverage with the three levels of governments in the implementation of the federalism reform in Nepal. Policy dialogue will cover all sectors.

Complementarity with other EU interventions

The federalism reform will directly impact the sectorial national strategies implementation, notably the Agriculture Development Strategy (ADS), the School Sector Development Plan (SSDP) and the Multi-Sector Nutrition Plan (MSNP).

The strengthening of capacities of the local authorities through the EU Federalism support will facilitate the data collection at local level and hence will help monitoring the other EU sectorial BS in the rural development and education focal areas of the current MIP (2014-2020).

Complementarity with funding under EU thematic budget lines

The EU funded projects under thematic budget lines implemented by CSO at grass root level will enable to fuel the EU policy dialogue with the three levels of governments.

In 2018, grants were awarded under the Civil Society-Local Authority (CSO-LA) in order to complement the EU Federalism Support:

- Under CSO, the EU Delegation had allocated a total amount of EUR 3 million in three grants to three NGOs under the theme "Enhancing citizens' participation in sub-national good governance in the context of the new federal system in Nepal" in provinces 2, 6 and 7 for a 4 years implementation period.
• Under LA, the EU Delegation had allocated a EUR 2 million grant with the Town development fund, public institution under the Ministry of Urban development to reinforce financial and technical capacities of 15 municipalities for a 4-year implementation period.

4.3 Mainstreaming

**Gender:** The EU strongly commits to promoting gender equality and empowerment within and beyond the EU, in particular through implementation of the Gender Action Plan (GAP) II. The transversal nature of the federalism support programme, poses an opportunity to effectively engage in policy dialogue with the government on gender equality questions, actively support women representatives in their new political roles, working with men representatives on creating and safeguarding enabling environment for women, as well as ensure the effective implementation of government policies and programmes at the local level following GESI commitments and guidelines.

**Resilience/conflict sensitivity:** The action entails a conflict prevention and peacebuilding dimension. The 2015 Constitution was a political settlement ending the ten years long conflict that prevailed in the country. Federalism state structure has been selected as the model of governance that will bring peace and stability to Nepal. By empowering the sub-national levels of governments, this programme will help the voice of citizens to be heard and their needs to be adequately fulfilled by the provincial and local public administration. The participatory and inclusiveness approach of this program will mitigate the risk of conflict and increase resilience at provincial and local levels. Indeed, conflict prevention can only be effective through meaningful inclusion.

**Environment and climate change:** This intervention will strengthen local governments and the participation of communities in local governance processes for planning, implementing and monitoring of investment in the environment and climate change related activities. More investments are needed on climate resilience infrastructures and disaster risk reduction, both at local and national levels. For instance, reinforcing the Build back better principles at local level will prevent damages caused by earthquakes.

**Right of indigenous people:** By empowering local governments, PLGSP will enable the representation and respect of rights of the indigenous peoples as well as and addressing root causes of conflict such as land issues.

**Disaster Risk Management:** By empowering local governments, PLGSP will enable the local governments to implement the National strategy for disaster risk management in agreement with the 2017 Disaster risk and management Act.

4.4 Contribution to SDGs

This intervention is relevant for the 2030 Agenda. It contributes primarily to the progressive achievement of SDG 16 on Peace and strong institutions, and will tackle the SDGs 17 on Partnerships and SDG 5 on Gender equality.

5. IMPLEMENTATION

5.1 Financing agreement

In order to implement this action, it is foreseen to conclude a financing agreement with the partner country.
5.2  Indicative implementation period

The indicative operational implementation period of this action, during which the activities described in section 4 will be carried out and the corresponding contracts and agreements implemented, is 54 months from the date of entry into force of the financing agreement.

Extensions of the implementation period may be agreed by the Commission’s responsible authorising officer by amending this Decision and the relevant contracts and agreements.

5.3  Implementation of the budget support component

5.3.1  Rationale for the amounts allocated to budget support

The amount allocated for the budget support component is EUR 28 000 000, and for complementary support is EUR 4 350 000. Through the amount allocated for budget support, the EU will represent the main donor for PLGSP. It will give EU leverage in terms of policy dialogue and influence on PLGSP. The complementary support is divided in EUR 2 000 000 as indirect management through an administrative agreement with the WB to top-up the EU contribution to the Multi-Donor Trust Fund on PFM Reform programme and in EUR 2 000 000 as indirect management through contribution agreement with the international organisation that will be chosen as technical assistance service provider in PLGSP. An amount of EUR 350 000 is allocated for technical assistance in statistics, evaluation, audit and communication and visibility.

5.3.2  Criteria for disbursement of budget support

a) The general conditions for disbursement of all tranches are as follows:
   - Satisfactory progress in the implementation of PLGSP, the related Performance Assessment Framework (PAF) and continued credibility and relevance thereof, or successor strategy;
   - Maintenance of a credible and relevant stability-oriented macroeconomic policy or progress made towards restoring key balances;
   - Satisfactory progress in the implementation of reforms to improve public financial management, including domestic revenue mobilisation, and continued relevance and credibility of the reform programme;
   - Satisfactory progress with regard to the public availability of accessible, timely, comprehensive and sound budgetary information.

b) The performance indicators for disbursement that may be used for variable tranches are listed as such:
   - Provincial Centre for Good Governance (PCGG) established and functional in all 7 provinces;
   - % of Local Governments (LGs) that have endorsed and implemented a GESI strategy approved by the Executive body;
   - % of Local governments that have capacity building plans based on Local Government Institutional Self-Assessment (LISA) report completed and communicated to PCGGs,
   - % of LGs that submit trimester financial statements to MOF/FCGO according to the national accounting standard;
   - % of LGs that have Revenue improvement action plans.

The chosen performance indicators and targets to be used for disbursements will apply for the duration of the action. However, in duly justified circumstances, the Ministry of Finance may submit a request to the Commission for the targets and indicators to be changed.
Note that any change to the targets should be agreed ex-ante at the latest by the end of the first quarter of the assessed year. The agreed changes to the targets and indicators shall be agreed in advance and may be authorised in writing (either through a formal amendment to the financing agreement or an exchange of letters).

In case of a significant deterioration of fundamental values, budget support disbursements may be suspended, reduced or cancelled, in accordance with the relevant provisions of the financing agreement.

### 5.3.3 Budget support details

Indicative breakdown and timetable of disbursement (EUR):

<table>
<thead>
<tr>
<th>Indicative Timing</th>
<th>Q2 2021</th>
<th>Q2 2022</th>
<th>Q2 2023</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed tranche</td>
<td>8 000 000</td>
<td>5 000 000</td>
<td>5 000 000</td>
</tr>
<tr>
<td>Variable tranche</td>
<td>0</td>
<td>5 000 000</td>
<td>5 000 000</td>
</tr>
<tr>
<td>Total</td>
<td>8 000 000</td>
<td>10 000 000</td>
<td>10 000 000</td>
</tr>
</tbody>
</table>

Budget support is provided as direct untargeted budget support to the national treasury. The crediting of the euro transfers disbursed into Nepali Rupees will be undertaken at the appropriate exchange rates in line with the relevant provisions of the financing agreement.

### 5.4 Implementation modalities for complementary support to budget support

The Commission will ensure that the EU appropriate rules and procedures for providing financing to third parties are respected, including review procedures, where appropriate, and compliance of the action with EU restrictive measures.

#### 5.4.1 Indirect management with an international organisation: PLGSP Technical Assistance

A part of this action may be implemented in indirect management with an entity that will be selected by the Commission’s services using the following criteria:

- Internationally recognised expertise; extensive working experience in supporting federalism implementation and local governance capacity building, in the country and internationally;
- Sufficient logistical and management capacities in Nepal to deploy nationwide;
- Managerial capacity, expertise and long-standing experience and credibility in directly implementing and liaising with relevant stakeholders in Nepal;

Selection will be made in close consultation by the government and in agreement with development partners co-financing the programme for provision of technical assistance support to PLGSP implementation.

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5 www.sanctions map.eu. Please note that the sanctions map is an IT tool for identifying the sanctions regimes. The source of sanctions stems form legal acts published in the Official Journal (OJ). In case of discrepancy between the published legal acts and the updates on the website it is the OJ version that prevails.
The implementation by this entity entails contributions to the achievement of the overall objective and the three specific objectives specified in section 4.1 - Support to PLGSP.

In case the envisaged entity would need to be replaced, the Commission’s services may select a replacement entity using the same criteria. If the entity is replaced the decision to replace it needs to be justified.

5.4.2 Indirect management with an international organisation: Local level PFM capacity building through the Multi-Donor Trust Fund managed by the World Bank

A part of this action may be implemented in indirect management with the World Bank Group. This implementation entails support to the progressive strengthening of the effectiveness of selected PFM institutions and related procurement, systems and procedures at the federal and subnational levels as mentioned in section 4.1 of the document. It capitalises on the existing experience and relations established during the WB PFM MDTF to which the EU is a contributor since 2011.

The envisaged entity has been selected using the following criteria:

- Internationally recognised expertise; extensive working experience and institutional memory in providing PFM support in Nepal since the first MDTF established in December 2010;
- Sufficient logistical and management capacities in Nepal to deploy nationwide;
- Managerial capacity, expertise and long-standing experience and credibility in directly implementing the Multi-Donor Trust Fund that finances PFM programmes through joint-donor contributions.

Currently the World Bank is strategically best placed to add value to the EU's interaction with the GoN in the implementation of PFM programmes and enjoys the highest levels of access to senior Nepal stakeholders.

This implementation will contribute to the achievement to overall objective and specific objectives specified in 4.1 Overall objective, specific objectives, expected outputs and indicative activities, II – Support to Integrated Public Finance Management Reform Programme (IPFMRP).

In case the envisaged entity would need to be replaced, the Commission’s services may select a replacement entity using the same criteria. If the entity is replaced the decision to replace it needs to be justified.

5.4.3 Procurement

For a proper implementation, it will be necessary to carry out external reviews or data verification exercises to inform disbursement decisions and to contribute to strengthening the policy monitoring framework and national statistical systems. To this end, external technical assistance will be contracted in direct management.

5.5 Scope of geographical eligibility for procurement and grants

The geographical eligibility in terms of place of establishment for participating in procurement and grant award procedures and in terms of origin of supplies purchased as established in the basic act and set out in the relevant contractual documents shall apply, subject to the following provisions.

The Commission’s authorising officer responsible may extend the geographical eligibility on the basis of urgency or of unavailability of products and services in the markets of the countries concerned, or in other duly substantiated cases where the eligibility rules would make the realisation of this action impossible or exceedingly difficult.
5.6 Indicative budget

<table>
<thead>
<tr>
<th>Item</th>
<th>EU contribution (amount in EUR)</th>
<th>Indicative third-party contribution, in currency identified(^4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Budget support (cf section 5.3)</td>
<td>28 000 000</td>
<td></td>
</tr>
<tr>
<td>Complementary support</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PLGSP Technical Assistance composed of</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indirect management with an International Organisation (cf section 5.4.1)</td>
<td>2 000 000</td>
<td></td>
</tr>
<tr>
<td>Indirect management with the World Bank for the PFM Reform through MDTF (cf section 5.4.2)</td>
<td>2 000 000</td>
<td></td>
</tr>
<tr>
<td>Procurement (Direct management) (cf section 5.4.3)</td>
<td>100 000</td>
<td></td>
</tr>
<tr>
<td>Evaluation – cf section 5.9, Audit (cf section 5.10)</td>
<td>150 000</td>
<td></td>
</tr>
<tr>
<td>Communication and visibility (cf section 5.11)</td>
<td>100 000</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>32 350 000</td>
<td></td>
</tr>
</tbody>
</table>

5.7 Organisational set-up and responsibilities

Committees will be set-up at federal and provincial levels with the joint participation of GoN and DPs in most of them. The EU will be represented in the PLGSP committees - which will give considerable policy dialogue leverage to the EU on the federalism reform in the country as well as influencing decisions in PLGSP implementation process.

Two committees will be set up at federal level, the National Steering Committee (NSC), which provides guidance and promotes intergovernmental coordination and the National Execution Committee (NEC) which oversees the overall programme implementation. In plus, the Programme Coordination Unit (PCU) provides the technical assistance to the programme and coordinate the Provincial Programme Implementation Units (PPIU).

Two committees will be set up at provincial level, the Provincial Steering Committee (PSC) which will provide strategic guidance and the Provincial Coordination Committee (PCC) which will coordinate among the provincial and local governments. The Provincial Programme Implementation Unit (PPIU) in the office of the Chief Minister will provide technical support to the provincial and local governments within the respective province and be responsible for proper execution of the innovation partnership fund at the provincial levels.

\(^4\) The other donors to PLGSP are DFID (EUR 23.45 million), Norwegian Embassy (EUR 17.55 million), Switzerland cooperation (EUR 1.75 million).
The provincial centres for good governance (PCGG) will have four key sections: (i) Curriculum and Materials development section, (ii) Institutional capacity assessment section, (iii) Training, research, coaching and mentoring section and iv) Administration and finance section.

5.8 Performance and Results monitoring and reporting

The performance monitoring will be carried out yearly by the GoN jointly with the EU Delegation. With regard to the performance monitoring of the general conditions for disbursement eligibility criteria on Budget Support, the Ministry of Finance (MoF) will report on macroeconomic performance improvements in PFM and budget transparency. Assessment of variable tranche indicators and targets will be jointly done with the MOFAGA and MoF. Technical assistance is foreseen to revise the accuracy of the performance indicators and to contribute to strengthening the policy monitoring framework and national statistical systems. This technical assistance will be funded through direct management – procurement part of the budget.

The day-to-day technical and financial monitoring of the implementation of this action will be a continuous process, and part of the implementing partner's responsibilities. To this aim, the implementing partner shall establish a permanent internal, technical and financial monitoring system for the action and elaborate regular progress reports (not less than annual) and final reports. Every report shall provide an accurate account of implementation of the action, difficulties encountered, changes introduced, as well as the degree of achievement of its results (outputs and direct outcomes) as measured by corresponding indicators, using as reference the policy or reform action plan list.

The following monitoring arrangements will be used to support the management of PLGSP:
A monitoring & evaluation framework will provide the foundation for programme monitoring and a system of online reporting will be developed. A baseline survey will be undertaken at the start of PLGSP. After completion of the programme, an end-of-programme evaluation will be undertaken against the baseline indicators in order to evaluate the achievement of programme results. An independent Mid-Term Evaluation of PLGSP will be undertaken during the first quarter of the third year of the programme. Annual Monitoring and Evaluation Plan (AMEP) will be the basis for regular monitoring. Internal and third-party monitoring, peer review, independent evaluation, joint field visits, and, external quality assurance teams will be used.

The Commission may undertake additional project monitoring visits both through its own staff and through independent consultants recruited directly by the Commission for independent monitoring reviews.

5.9 Evaluation

Having regard to the nature of the action, a mid-term and final evaluation will be carried out for this action or its components via independent consultants contracted by the Commission.

Mid-term evaluation will be carried out for problem solving and learning purposes, in particular with respect to the intention to launch a second phase of the action.

Final evaluation will be carried out for accountability and learning purposes at various levels (including for policy revision), considering in particular the fact that it is a very complex programme involving several stakeholders and having considerable impact.
The evaluation of this action may be performed individually or through a joint strategic evaluation of budget support operations carried out with the partner country, other budget support providers and relevant stakeholders.

The Commission shall inform the implementing partner at least 30 days in advance of the dates foreseen for the evaluation missions. The implementing partner shall collaborate efficiently and effectively with the evaluation experts, and inter alia provide them with all necessary information and documentation, as well as access to the project premises and activities.

The evaluation reports shall be shared with the partner country and other key stakeholders. The implementing partner and the Commission shall analyse the conclusions and recommendations of the evaluations and, where appropriate, in agreement with the partner country, jointly decide on the follow-up actions to be taken and any adjustments necessary, including, if indicated, the reorientation of the project.

Evaluation services may be contracted under a framework contract.

5.10 Audit
Without prejudice to the obligations applicable to contracts concluded for the implementation of this action, the Commission may, on the basis of a risk assessment, contract independent audits or expenditure verification assignments for one or several contracts or agreements.

It is foreseen that audit services may be contracted under a framework contract.

5.11 Communication and visibility
Communication and visibility of the EU is a legal obligation for all external actions funded by the EU.
This action shall contain communication and visibility measures which shall be based on a specific communication and visibility plan of the Action, to be elaborated at the start of implementation.

In terms of legal obligations on communication and visibility, the measures shall be implemented by the Commission, the partner country, contractors, grant beneficiaries and/or entrusted entities. Appropriate contractual obligations shall be included in, respectively, the financing agreement, procurement and grant contracts, and contribution agreements.

The communication and visibility requirements for European Union external action (or any succeeding document) shall be used to establish the Communication and Visibility Plan of the Action and the appropriate contractual obligations.

It is foreseen that a contract for communication and visibility may be contracted.
### APPENDIX – INTERVENTION LOGIC TABLE (FOR BUDGET SUPPORT)\(^6\)

<table>
<thead>
<tr>
<th>Results chain</th>
<th>Indicators (max. 15)</th>
<th>Baselines (2018)</th>
<th>Targets by the end of the budget support contract (2023)</th>
<th>Sources of data</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Expected impact of the policy (Overall objective)</strong></td>
<td>To contribute to the creation of functional, sustainable, inclusive and accountable provincial and local government</td>
<td></td>
<td></td>
<td>MOFAGA/PLGSP Annual Report - annual report (September each year) including reporting progress on EU indicators</td>
</tr>
</tbody>
</table>
| **Expected outcomes of the policy (Specific objective(s))** | Objective 1: Government institutions and intergovernmental mechanism at all level are fully functioning in support of federal governance, as per the constitution  
Objective 2: Provincial and local governments have efficient, effective, inclusive and accountable institutions, and promote innovations and partnership for inclusive local development  
Objective 3: Elected representatives and civil servants at provincial and local governments have the capacity and serve citizens to their satisfaction | Primary – Federal and provincial - government expenditures as a % of original approved budget, by sector (Related to SDG 16.6.1)  
Government Effectiveness score **  
Extent of change in citizens perceptions of the quality and access to services * | 76 % (F)  
N/A (P) | 84.9 % (F)  
70 % (P) | MoF, NPC with support from PCU and PPIU.  
World Bank Worldwide Governance Indicators.  
Citizens survey |
| | | | 19 | 39 | |
| | | | None | 70% | |

\(^6\) Mark indicators aligned with the relevant programming document with "\*\*" and indicators aligned to the EU Results Framework with "**". Indicators used within variables tranches must be flagged in bold.
<table>
<thead>
<tr>
<th>Induced outputs</th>
<th>1A. Federal ministries and agencies are supporting the PLGs in policy and institutional spheres for implementing federal governance</th>
<th># number of federal agencies developed policy guidelines for local and provincial governments in facilitation with MOFAGA</th>
<th>0</th>
<th>10</th>
<th>MOFAGA/PLGSP Annual Report</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1B. Inter-governmental administrative mechanisms are fully functional</td>
<td># Coordination meeting between OPMCM, federal ministries and provincial governments’ focal persons</td>
<td>None</td>
<td>Quarterly</td>
<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td></td>
<td>2A. Provincial governments have functional, inclusive and accountable institutions</td>
<td>% LG that have conducted a ward level planning workshop to prepare their annual plan *</td>
<td>70%</td>
<td>100%</td>
<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td></td>
<td>2B. Local governments have functional, sustainable, inclusive and accountable institutions</td>
<td># PGs ministries and departments and institutions using a performance assessment system</td>
<td>None</td>
<td>7</td>
<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td></td>
<td>2C. Provincial and local governments promote innovations and partnership for inclusive governance and local development</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3A. Elected representatives and civil servants of provincial governments are capacitated to serve citizens to their satisfaction</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3B. Citizens are satisfied from the services of the capacitated elected representatives and civil servants of local governments</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

[25]
<table>
<thead>
<tr>
<th>Direct outputs</th>
<th>% of PGs and LGs adapt and adopt planning, budgeting procedure and tools developed by Federal level institution</th>
<th>% of total PGs annual budget allocated for capacity development</th>
<th>% LGs have capacity building plans based on LISA report completed and communicated to PCGGs</th>
<th>% of LGs that submit trimester financial statements to MOF/FCGO</th>
<th>Provincial Centre for Good Governance (PCGG) established in all 7 provinces and functional</th>
<th>7/753</th>
<th>MOFAGA/PLGSP Annual Report</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Federal Level institutions develop legislations and policies to support provincial and local governments.</td>
<td>none</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td>2. Federal level institutions develop tools and systems to support provincial and local Governments in a consultative process.</td>
<td>y1 US$ delivered by IPF to LG for y2 innovative projects in y3 provinces</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td>3. Inter-governmental administrative mechanisms strengthened and functional</td>
<td>% of PGs and LGs adapt and adopt planning, budgeting procedure and tools developed by Federal level institution</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td>4. Provincial Governments drafted legislation</td>
<td>% of total PGs annual budget allocated for capacity development</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td>5. Modernized Provincial Government systems enable horizontal and vertical accountability to all citizens and mainstream GESI</td>
<td>% LGs have capacity building plans based on LISA report completed and communicated to PCGGs</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td>6. Provincial Governments Manage core public Administration functions</td>
<td>% of PGs and LGs that submit trimester financial statements to MOF/FCGO</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td>7. PCGGs made operational to deliver capacity development services</td>
<td>Provincial Centre for Good Governance (PCGG) established in all 7 provinces and functional</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<td>MOFAGA/PLGSP Annual Report</td>
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<tr>
<td>8. Modernised Local Governments have strong administrative system, accountable and public financial management system</td>
<td>MOFAGA/PLGSP Annual Report</td>
<td>0</td>
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<td>MOFAGA/PLGSP Annual Report</td>
</tr>
<tr>
<td>9. Local Government systems enabled horizontal and vertical Accountability to all citizens</td>
<td>MOFAGA/PLGSP Annual Report</td>
<td>0</td>
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<tr>
<td>10. Local Governments systems mainstream GESI in their service delivery</td>
<td>MOFAGA/PLGSP Annual Report</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<td>MOFAGA/PLGSP Annual Report</td>
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</tbody>
</table>

yy1: US$28 M in 2021/22 and US$ 35 M in 2022/23

50% in 2019/20
100% in 2020/21

70%

90%

7
| 11. | Local Governments systems enable citizen engagement and inclusive participation |
| 12. | Innovation and Partnership fund is operational and transparently supporting local governments innovative practices |
| 13. | Elected Representative and Civil servants at the province level are incentivized and trained for delivering high quality services |
| 14. | Local Governments’ elected representative and civil servants are empowered and trained for delivering high quality services |

| % LGs have endorsed a GESI strategy approved by the Executive Body | 4% | 70% | MOFAGA/PLGSP Annual Report |
| % of LGs that have Revenue Improvement Action Plan | 20% | 60% | MOFAGA/PLGSP Annual Report |