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Inter-American Development Bank

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RE-293

The Project Supervision System: An Evaluation of use of its instruments

Office of Evaluation and Oversight

Officially distributed to the Board of Executive Directors on April 13, 2004.

CONTENTS

ANNEXES

ABBREVIATIONS

APE	Annual portfolio review by the Country Office
AS	Project assumptions
ASB	High probability that project assumptions will hold true
ASM	Low probability that project assumptions will hold true
AUG	Office of the Auditor General
BEP	Borrower's ex-post evaluation
BIS	Bank for International Settlements
CDD	Actual date of final disbursement
CMI	Completeness Monitoring Index
CO	Country Office (of the Bank) Policies governing the operation of Country Offices
CPE	Country program evaluation
CPR	Annual portfolio review mission
DO	Development Objectives (of the project)
DOB	Classification probable or highly probable that development objectives will be met
DOM	Classification low probability or improbable that development objectives will be met
DoA	Date of loan approval by the Board of Executive Directors
DoS	Date of signature of loan contract
DoEf	Date operation in execution becomes effective (parliamentary ratification)
DoE	Date of eligibility for disbursements
DoID	Date of first disbursement
EFA	External Financial Audit of loans
FIN	Ex post evaluation by Bank
IP	Project implementation
IPB	Project implementation progress satisfactory or highly satisfactory
IPM	Project implementation progress unsatisfactory or very unsatisfactory
IVF	Institutional and Financial Inspection Visits
IVT	Technical Inspection Visits
LAM	Loan Administration Missions
LMS	Loan Management System
MA	Annual Review or Administration Mission
MDB	Multilateral development bank
MMT	Midterm Review Mission
MSP	Specific Mission
OA	Monitoring, Support and Evaluation Policies for Bank Operations
OCMI	Overall Completeness Supervision Index
ODD	Original date of final disbursement
OR-AUG	Administrative and Operational Review of Country Offices by AUG
PAIS	Project Alert Identification System
PBL	Policy-Based Loan

PCR	Project Completion Report
PPMR	Project Performance Monitoring Report System
RE	Regional Operations Departments
ROS	Office of Regional Operations Support
SEP	Project Implementation Supervision System
SM	Startup Mission
SRM	Sector Portfolio Review Mission

EXECUTIVE SUMMARY

A. Conclusions

Supervision at the IDB serves two main purposes. It provides the Board of Executive Directors and Senior Management with the means of managing the risks that affect Bank-financed operations and determines the extent to which such operations contribute to the accomplishment of the institution's development goals.

Various factors exist to explain why the objectives of project supervision are often not accomplished. The main reasons are: i) supervision may not have been carried out or reports may not have been prepared in accordance with Bank policies and standards; ii) risk management (anticipation, evaluation, and mitigation) is not always an essential component in the context in which the supervision function is performed; and iii) the instruments used for supervision do not bring the added value or include the procedures for managing the risks.

The present evaluation[1] focuses on the first two groups of factors: namely, the use of supervision instruments, and assess the extent to which they comply with the requirements established in Bank manuals and standards, and to determine how these instruments relate to the management risks associated with the execution of operations and to the internal control systems.[2]

An analysis was carried out to learn how well the supervision instruments that are available are understood and how they are applied, using specific methods that would make it possible to ascertain whether an understanding of this strategic function exists at the Management level and the depth of this understanding.

1. The present evaluation found that:

- There is no single document that consolidates all information on supervision instruments and the functioning of the supervision system, a factor that militates against a general understanding of their use as well as their limitations.

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[1] The conceptual and methodological aspects of this evaluation are presented in the main body of the text and in Annex A.

[2] Part of OVE's work program includes regular evaluations of the elements of supervision instruments and their use. The following documents provide useful background on this aspect of OVE's work: RE-247 "Oversight Review of the IDB's Project Supervision Review, the Midterm Evaluation and the Project Completion Report", OVE, April 2001; RE-260 "Development Effectiveness Report", OVE, February 2002; RE-275 "Analysis of Project Evaluability, Year 2001", OVE, January 2003; and the CPEs produced by OVE in the last three years, which have been contributing to the analysis of project execution, the degree of compliance, and the quality of IDB supervision in its borrowing member countries.

- The supervision instruments seemed to have been designed to accommodate information requirements and not the requirements of the decision-making process associated with portfolio management risk evaluation.[3]

- Without an institutional risk management function, there can be no basis from which to monitor risk, thus making the supervision system inconsistent and ineffective, with a focus on mitigating, not anticipating, risk.

- The absence of a risk supervision approach means that the emphasis on mandatory supervision is the same for all operations. This makes the system less cost-effective, which in turn affects the principle of economy in the use of scarce resources.[4]

- Supervision as it stands has been divided into separate instruments that are neither sequenced nor integrated. Moreover, there is no explicit methodology describing how these instruments are to be applied and how they relate to one another during project execution.

- The Bank's risk management instruments are not systematically organized, thus diminishing the impact of the institution's extensive efforts to bolster the many different, and sometimes redundant instruments, it has at its disposal.[5]

- Databases are inadequate, are spread around in different places and file forms, are not updated, and are not organized to fully satisfy the decision-making requirements of the Board of Executive Directors and Senior Management.

- There is no independent and systematic internal control to monitor project execution or the effectiveness with which official Bank supervision instruments have been applied.[6]

- The instruments reviewed show a degree of compliance 25% below the levels stipulated in Bank policies and manuals.

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[3] The Bank faces three types of risks: those associated with fulfilling its mission (development risks); those associated with shortcomings in the oversight environment and the application of standards and procedures governing the use of resources in member countries (fiduciary risks), and those associated with administrative capacity for project implementation (operational risks). Such risks may be rooted in factors endogenous or exogenous to the cycle of operations, forming part of the assumptions of the operation.

[4] If there is no relationship between supervision and the risk, when any risks do arise, the problems are associated with a failure to complete activities in the case of projects with fewer risks, which paradoxically means that Bank policies and standards are not observed.

[5] These efforts have been remarkably successful in terms of improving the range of instruments available (mainly the PPMR, the PCR, and more effective use of MS).

[6] The AUG is an integral part of the Bank's oversight system, serving to monitor the Country Office financial and operational management controls. It does not come under the internal controls for project supervision insofar as supervision is not systematic. It only reviews and evaluates the effectiveness and efficiency of the country financial and operational management procedures.

- No formal framework or standards are employed to certify the effectiveness of internal controls in verifying that loan resources are used for the purposes for which they were approved.

2. Based on the foregoing, the principal conclusions are:

- The Bank does not have an integrated and independent supervision system to anticipate risk. This renders management of much of the portfolio and the Bank's decision-making process ineffective.

- As there is no formal system of consolidated supervision, it is not clear who is responsible for risk supervision and management and how the different instruments relate to one another.

- Because project management is not based on risk assessment, the supervision instruments that exist are inconsistent with the supervision function and therefore inefficient and less cost effective.[7]

- There is no integrated, transparent, and readily accessible information system that can be used to anticipate and manage risk as well as to verify the extent to which supervision and internal control functions have been fulfilled.

- The Board of Executive Directors and Senior Management are not kept regularly informed on these specific issues.
- That shortcomings have been identified in the present system does not mean that the Bank does not monitor its operations but that institutionally, supervision is ineffective.
- As supervision is based mainly on mitigating contingencies as they arise, the procedures set out in Bank manuals and standards are not fulfilled and mechanisms not formally approved but considered more suitable by Management to correct such contingencies come into play. Paradoxically, such mechanisms are virtuously associated with the risk-based supervision function.[8]

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[7] The mandatory supervision instruments are compulsory for all operations, and are accorded equal importance with a similar level of risk in all operations, which minimizes the impact of the risks on portfolio management.

[8] In fact, empirical analysis suggests that the project supervision carried out is related to the ad hoc organization of supervision in response to risks effectively produced, given their essentially mitigatory nature. This situation is also associated with broadening the boundaries and the informal nature of the supervision system, based on the use of informal or other supervision procedures considered to be more effective than the mandatory ones. Such procedures are not thrown together systematically in the institution's formal supervision instruments or stored in standard information technology databases. This makes the system less formal and creates an environment that does not lend itself to fulfillment of supervision commitments.

3. The Bank's present supervision system is not in line with the best practices of other multilateral development banks, bilateral aid agencies, and governments in the member countries. In recent years, these bodies have been incorporating various practices to improve the quality of management and internal control supervision as well as coordination of such controls with institutional objectives. The following points should be noted:

- Risks that prevent the institution's strategic objectives from being accomplished need to be identified and analyzed for guidance in designing and managing operations, thus adding at the same time to the effectiveness of supervision.

- A formal framework or standards of internal control should be employed to ensure that the functions and responsibilities associated with execution and supervision are consistent and are coordinated in accordance with the institution's strategic objectives and policies.

- Responsibility for institutional supervision functions relating to project execution, independent of risk management, is important in order to ensure compliance with management guidelines, mandates, and standards.

- Regular outside supervision of internal controls is needed to certify that such supervision is adequate and that the objectives sought are being achieved.

- The information needed for proper performance of supervision functions in the context of risk-based management must be systematically organized, timely, and user-friendly.

B. Recommendations

On the basis of these findings, the following recommendations are made:

- Develop an integrated execution supervision system, based on a risk-based portfolio management approach that incorporates the best practices of other similar institutions.[9]

- Adopt an internal control framework model to improve governance within the Bank itself.

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[9] Material references to this topic may be found in various documents developed by the "Basel Committee on Banking Supervision" and the BIS; the Asian Development Bank's "Handbook for Integrating Risk Analysis in the Economic Analysis of Projects," in papers by the World Bank's OED, and several relating to risk assessment by the World Bank, as well as by other government agencies in Australia, the United Kingdom, and the United States. Private international consulting and auditing firms, such as Ernst & Young and Deloitte Touche Tohmatsu, have also made significant contributions to the topic.

- Prepare a report, on a regular basis, to be presented to the Board of Executive Directors and Senior Management establishing the progress made in terms of i) the effectiveness of operations in contributing to the institution's strategic objectives and the extent to which its policies and standards have been observed; ii) management effectiveness based on risk evaluation and execution supervision; and iii) the cost efficiency of management control and institutional supervision systems.

- Develop an integrated reporting system as a key component of the supervision system to support the recommendations noted earlier and to provide Bank staff with on-line information and guidance on the performance of management, supervision, and execution supervision functions.

I. INTRODUCTION

A. Background

1.1 Under Bank policy (document RE-238), the responsibilities entrusted to the Office of Evaluation and Oversight (OVE) include supervision of the systems for evaluation of operations with borrowers.

1.2 In fulfilling this role, in April 2001, OVE presented a report entitled, "Oversight review of the IDB's project monitoring review, the midterm evaluation, and the project completion report" (document RE-247). This report looked at the content and quality of three instruments used in project execution supervision.

1.3 When document RE-247 was discussed, Management suggested that OVE broaden its review to cover all of the instruments in the supervision system.[10]

1.4 Since the Bank's reorganization in 1994, reaffirmed in 1996, emphasis has been placed on the Regional Operations Departments' responsibility for project management and on accountability targeted on output impact. Primary responsibility for project management falls to the Country Offices, which report to the Regional Operations Departments. The Regional Operations Departments consolidate supervision of all matters relating to the activities of staff engaged in project management.

1.5 Reporting based on decentralized supervision is carried out through a series of supervision instruments. These instruments require staff assigned to operations administration and control to identify any problems encountered with project implementation, and to make recommendations on how execution can be improved.[11]

1.6 Before an evaluation is performed, the instruments that will be used to supervise project execution are identified. This step would call for a detailed analysis of the process of supervision, in order to make a distinction between the instruments of supervision and the inputs used to produce them.

1.7 One initial obstacle encountered is that there is no single document in which the process of project supervision employed by the Bank is described comprehensively.

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[10] The comments made by Management on 7 June 2001 noted in particular: "The report (RE-247) presents a partial analysis of the Bank's overall monitoring system. The issues regarding monitoring and reporting are limited to certain instruments such as PPMRs, PCRs and MTEs. In order to assess the system as a whole, the report must take into account: country portfolio reviews, sector portfolio reviews, administration missions (other than MTEs), project inspection visits, financial audits, etc. Although the document mentions these other instruments (p. 1.9), it fails to address the continuous follow-up that these instruments provide. Many of the shortcomings attributed to the PPMR system cited in the report are precisely covered by the rest of the monitoring tools. Failure to recognize this leads to an inaccurate assessment of the system."

[11] See Annex A.

The information that exists is found dispersed in different manuals, policies, and standards, which have been added to and updated over time as problems are detected and lessons learned from project execution.

1.8 From a review of Bank manuals and a survey of the staff charged with these responsibilities it emerged that some of the instruments used for supervision are not spelled out in specific standards and that interpretations differ as to the scope of supervision. It was also found that, although the staff surveyed feel they are part of the entire process, interpretations differ from one individual to another without a collective understanding of what the current version is.

1.9 Furthermore, the focus of the manuals, guidelines, etc. used for supervision has been to describe the activities involved, not to give a clear overall picture of the process. It is difficult, therefore, to distinguish between the instruments and the inputs that are required. The present manuals describe the instruments, but not the purpose of each activity and how they relate to one another.[12]

1.10 Annex A sets out the conceptual and methodological framework used for identifying the instruments that will be used for supervision of project execution and the project outputs. These instruments share the unique feature of being instruments used by Management to identify and analyze the risks emanating from project execution and to report on how such risks are managed.

1.11 In an institution such as the Bank, these risks are linked mainly to: (i) the probability of achieving a project's development objectives with the approved resources; (ii) the institutional capacity to disburse the loans by prescribed deadlines and in accordance with contractual conditions; and (iii) the use of funds according to established procedures, and for the purposes for which they were approved.

1.12 The present evaluation is based on 16 supervision instruments identified in the application of the methodological procedures. These instruments differ in periodicity and scope, and according to the type of operation. For purposes of consistency, the study considered all of these different dimensions. That the analysis confined itself to supervision instruments does not mean that the author was unaware of other activities involved in supervision or of ongoing actions carried out by the Country Offices in conjunction with the executing agencies. Such supervision activities are inputs for the instruments being considered that should normally be incorporated into the process. At this stage, however, supervision of this kind has been considered to fall outside the scope of the present evaluation, but will be taken up in a subsequent work.

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[12] Operations Administration policy OP-306 sets guidelines for five general action guides and defines the operational content of the supervision that will then be specified in the Operations Manual and Country Office Manual.

B. Object and scope of the study

1.13 This study serves two main purposes. First, it gauges the extent to which the supervision instruments used by Management fulfill their functions, indicating how the Bank's project execution supervision system (SEP) was employed for supervision of outputs and dialogue with the national authorities, in which their views were expressed. Second, it shows how the SEP is used to monitor project execution risk management, by verifying whether the system is able to manage and anticipate risks and furnish solutions when problems do arise, and whether these solutions can be supervised.

1.14 The evaluation of the quality of existing information on supervision, in terms of access, reliability, and data quality, as well as the extent to which it can be updated to user demands was an essential part of the analysis.

1.15 No attempt is made to analyze the quality of each supervision activity, nor to suggest that the system be redefined.[13] A baseline was established to show the condition of information as it now stands and the use of the SEP, and tests were performed to see whether those responsible for supervision and decision making are familiar with the instruments of supervision and their prescribed use (asymmetry of execution information).

1.16 As part of its work program, OVE performs periodic evaluations of supervision activities and the use of supervision. Relevant background information is found in the following reports: Oversight Review of the IDB's Project Monitoring Review, (document RE-247); the Midterm Evaluation and the Project Completion Report (document RE-247); Development Effectiveness Report (document RE-260); Analysis of Project Evaluability, Year 2001 (document RE-275); and the CPEs produced by OVE during the last two years, which devote some time to looking at program implementation, degree of compliance, and the quality of the components of supervision.[14]

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[13] The methodology used focuses on the monitoring outputs or instruments instead of on the project's products, because Bank documents contain little information on such products as well as on the devices required for execution risk management.

[14] A recent study (document GN-2262), "Review of the Quality at Entry of projects approved by the Board of Executive Directors from August through December 2002", confirms concerns about the content of original project designs. The study notes that, in a review of 30 projects, a significant number had problems with establishing baselines and indicators for monitoring outcomes, with identifying and mitigating the totality of risks affecting the achievement of project results, and with the inadequate attention paid to monitoring the actual benefits of projects after their implementation.

C. Working methodology

1.17 The years 1998 to 2001 were selected for the analysis[15] because they conform to the system of supervision in effect. This is a representative period that makes it possible to describe the nature and trends of the current supervision system while avoiding the risk of encountering exceptional circumstances.

1.18 Projects or loans in all borrowing countries were analyzed. The analysis covered virtually all types of loans in execution during that period so that an initial baseline could be constructed for the study that would serve to establish indicators showing how the system of supervision has evolved.

1.19 The operations not included in the analysis were private sector development program loans (PPRV), preinvestment loans (PGPR), emergency reconstruction facility loans (PERF), and emergency sector loans (PEMG).

1.20 Operations in progress were considered to be those approved by the Board of Executive Directors during the period under review as well as those prior to that period having their last disbursement after 1 January 1998. The resulting sample consisted of 616 operations, in an aggregate amount of US$50.6 billion. The year 2002 was added to aid with the analysis of development objectives and financial supervision.

1.21 The projects were grouped by number, loan number, amount, sector, type, description, country, and region. The database includes key dates relating to the supervision cycle, in order to be able to determine the coverage of each supervision tool based on the extent to which it varied from those dates.

1.22 While this report uses information that is aggregated or organized into categories in order to draw its conclusions, the database of detailed information is available for consultation and use in subsequent analyses.

1.23 In quantifying and evaluating the Bank's monitoring and supervision activities for operations in progress, a series of indices and indicators were selected, and these are defined and justified in each chapter in which they are used.

1.24 The 16 supervision tool selected (see Annex A) did not include: sector portfolio review missions (SRM), which apply only to a small proportion of the projects in

[15] The chapter on the evaluation of supervision as a risk-management system includes an analysis for the year 2002.

the sample, and would therefore contribute little to the analysis[16]; and annual portfolio evaluations (APE) conducted by the COs, which are general portfolio reports and do not refer to individual projects, but are very similar to the CPRs in content. Specific missions (SPM) are grouped under the annual review missions (MA) for purposes of this analysis.

1.25 The evaluation focused on assessing, at face value, the degree to which the supervision instruments that document execution activities and outcomes compare to what was expected in Bank manuals or standards. The evaluation was supplemented with an analysis of how supervision instruments are used to manage project execution risk.

1.26 The empirical analysis underlying this evaluation was based on information produced or supplied by the Regional Operations Departments (RE).

D. Layout of the report

1.27 This evaluation has been divided into six chapters. Chapter II assesses the functioning and management of the supervision information system, and how effective it is for management.

1.28 Chapter III evaluates the extent to which supervision activities fulfill the goals set out in Bank policies and regulations.

1.29 Chapters IV and V look at how the Bank supervises project execution risks. Chapter IV examines the supervision of fiduciary risk involved in project execution, and Chapter V the supervision of development risks.

1.30 Chapter VI examines the way in which the Bank administers supervision, and anticipates and mitigates development risks. Lastly, presented in Chapter VII are the findings of the evaluation and its recommendations.

II. THE SUPERVISION INFORMATION SYSTEM

2.1 This chapter describes how information on supervision instruments identified is organized, in terms of accessibility, reliability, and data quality, and the extent to which it can be adapted to user demands. Insofar as the information requested is historical, the analysis serves to size the problems and gauge the progress made in addressing them.

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[16] A total of 42 SRMs were performed for the entire period. SRMs were performed in only 19 of the 26 borrowing countries, with five countries (Venezuela, Colombia, Brazil, Argentina, and The Bahamas) accounting for nearly 60% of such missions. SRMs were performed in 13 sectors, of which five account for 74% of those missions (agriculture, drinking water and sanitation, infrastructure, education, and health).

2.2 Right from the start, it was found that, for the Bank as a whole, only seven of the 16 supervision instruments provide information on execution (CPR, PPMR, PCR, APE, PAIS, EFA, and OR-AUG), with some gaps, and of those, six currently offer centralized information online.

2.3 Information on the remaining instruments was not initially available, which meant that it had to be obtained from the Operations Departments which prepared it on the basis of their records, a factor that led to delays in building a comprehensive database. The delays ranged from 49 to 217 days, depending on the type of tool and the region.

2.4 Efforts then turned to reviewing, standardizing, and ordering the information received, in terms of the role it plays in the cycle of project supervision. Only 28% of the instruments, from various sources, did not require subsequent clarification. All of the information received demanded additional processing in order to complete the task of attestation—verifying the extent to which the instruments are used in accordance with Bank regulations and policies.

Table 1
Survey and evaluation of information on project implementation monitoring
Transactional costs associated with the availability of basic information

			Centralized information		OVE survey				Evaluation of information		
Monitoring tool	Bank policies	Responsibility center	Available at startup	Information online	Date of request	Addressee	Date of initial response	Origin of response	Time required, including clarifications (days)	Clarification required	Adjustments required to verify compliance
Internal											
MS	OA-222	RE	0	0	20-Jul-01	RE1	10-Sep-01	RE1	52	0	1
					20-Jul-01	RE2	07-Sep-01	RE2	70	1	1
					20-Jul-01	RE3	12-Sep-01	RE3	54	1	1
MA	OA-222	RE	0	0	20-Jul-01	RE1	10-Sep-01	RE1	77	1	1
					20-Jul-01	RE2	07-Sep-01	RE2	70	1	1
					20-Jul-01	RE3	12-Sep-01	RE3	54	1	1
MSP	OA-222	RE	0	0	20-Jul-01	RE1	10-Sep-01	RE1	52	0	1
					20-Jul-01	RE2	07-Sep-01	RE2	70	1	1
					20-Jul-01	RE3	12-Sep-01	RE3	54	1	1
MMT	OA-222	RE	0	0	20-Jul-01	RE1	10-Sep-01	RE1	52	0	1
					20-Jul-01	RE2	07-Sep-01	RE2	70	1	1
					20-Jul-01	RE3	12-Sep-01	RE3	54	1	1
SRM	OA-224	RE	0	0	…	…	…	…		…	…
CPR	0A-223	RE	1	1	On line	SEC	On line	SEC	0	0	0
IVT	CO-204/CO-308	CO	0	0	20-Jul-01	RE1	10-Sep-01	RE1	52	1	1
					20-Jul-01	RE2	19-Feb-02	RE2	217	1	1
					20-Jul-01	RE3	12-Sep-01	RE3	54	1	1
IVF	CO-204/CO-308	CO	0	0	20-Jul-01	RE1	10-Sep-01	RE1	52	1	1
					20-Jul-01	RE2	19-Feb-02	RE2	217	1	1
					20-Jul-01	RE3	12-Sep-01	RE3	54	1	0
PPMR	CO-303	CO	1	1	On line	OPS	On line	OPS	0	0	1
PCR	CO-205	CO	1	1	On line	OPS	On line	OPS	0	0	1
APE	OA-230/CO-302	CO	1	1	22-Oct-03	ROS/PMP	23-Oct-03	ROS/PMP	1	…	…
FIN	CO-205	CO	0	0	18-Jul-02	RE1	05-Sep-02	RE1	63	1	1
					18-Jul-02	RE2	24-Oct-02	RE2	98	0	1
					18-Jul-02	RE3	16-Oct-02	RE3	90	1	1
PAIS	Function	ROS/PMP	1	1	On line	ROS/PMP	On line	ROS/PMP		0	1
External											
EFA	OA-419/AF-100	CO	1	1	On line	ROS/PMP	On line	ROS/PMP	0	1	1
BEP	OA-242/CO-205	CO	0	0	18-Jul-02	RE1	05-Sep-02	RE1	49	1	1
					18-Jul-02	RE2	24-Oct-02	RE2	98	0	1
					18-Jul-02	RE3	16-Oct-02	RE3	90	1	1
OR-AUG	Function	AUG	1	0	In OVE	AUG	In OVE	AUG	0	…	…

Notes:
1. Where the time required exceeded the periods indicated, this is explained by the additional days needed to supplement or clarify the original information.
2. In the colums in which the binary system was used, 0 and 1 indicate the absence and presence, respectively, of the attribute considered in each case.

2.5 Following is a summary, by type of tool, of the major information problems encountered in attempting to establish the analytical database.

Table 2
Classification of major information problems relating to supervision instruments

Tool	Major problems encountered
MS	1. To construct the inventory of planned missions, all projects in execution had to be reviewed. 2. The information received on missions conducted could not be distinguished from other missions. 3. There is no inventory of missions conducted to help in verifying compliance. **4. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
MA	1. To construct the inventory of planned missions, all projects in execution had to be reviewed. 2. The information received on missions conducted could not be distinguished from other missions. 3. There is no inventory of missions conducted to help in verifying compliance. **4. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
MSP	1. To construct the inventory of planned missions, all projects in execution had to be reviewed. 2. The information received on missions conducted could not be distinguished from other missions. 3. There is no inventory of missions conducted to help in verifying compliance. **4. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
MMT	1. To construct the inventory of planned missions, all projects in execution had to be reviewed. 2. The information received on missions conducted could not be distinguished from other missions. 3. There is no inventory of missions conducted to help in verifying compliance. **4. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
IVT	1. Information is not systematic and is available only at the CO level. 2. Delivery of information is not standardized: some COs report by project, others by officer, others do not distinguish between IVT and IVF. **3. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
IVF	1. Information is not systematic and is available only at the CO level. 2. Delivery of information is not standardized: some COs report by project, others by officer, others do not distinguish between IVT and IVF. **3. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
PPMR	**1. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.** 2. The database uses nonstandard criteria that impede verification: cancellations and terminations are not recorded, assuming the customary rule that no PPMR is done if a PCR is performed.
CPR	**1. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
PCR	**1. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**
FIN	1. There is no inventory of missions planned and performed to help in verifying compliance. **2. There are no time-specific routines for monitoring the degree of compliance with Bank**

Table 2
Classification of major information problems relating to supervision instruments

Tool	Major problems encountered
	regulations
BEP	1. There is no inventory of missions planned and performed to help in verifying compliance. **2. There are no time-specific routines for monitoring the degree of compliance with Bank regulations**
EFA	1. Online information is not sufficiently systematic to certify compliance. 2. It is produced at the loan, not the project, level, which introduces contradictions since some operations are done at the project level (multi-stage or with components in other separate loans). **3. There are no time-specific routines for monitoring the degree of compliance with Bank regulations**
PAIS	**1. There are no time-specific routines for monitoring the degree of compliance with Bank regulations.**

2.6 Some preliminary conclusions can be drawn from the foregoing. The expectation of being able to construct quickly an integrated database suitable for evaluating needs, incorporating feedback, and capturing information on a specific item from different sources, was unrealistic. Construction was slow, the original information was incomplete, and successive adjustments were needed to make it usable and reliable so that it could be adapted to the purposes of the study.

2.7 There is no central information system for comprehensive monitoring of all supervision instruments, although the standard and repetitive nature of the products would make this advisable. The different products, with the exception of the PPMR, PCR and EFA, function as isolated lists of information, based in some cases on their own formal design, and are not supported with an electronic file. Information technology designs and procedures do not function as local networks connected to a relational central database with standard outputs for independent access and production of reports based on this information. Only the PPMR, the APE and the EFA have associated applications to support the Bank with the task of supervision.

2.8 For virtually all of the supervision instruments, information is not ordered according to procedures that reflect the different time frames to which each tool applies. This limitation in the information system makes it difficult to verify that Bank policies and regulations have been observed. That is why a special database that could verify this point needed to be constructed for the evaluation.

2.9 Information is organized by product type and not as a system integrated into Management's decision-making process. This means that information does not have to be up to date, and therefore, usable for monitoring the effectiveness of supervision in accordance with established deadlines and protocols. The process of supervision is tailored to the information needs of Management, and not to a system that can identify and resolve problems on a timely basis.

2.10 That information consists of isolated files rather than a management system is also attributable to the absence of a system manager, for the Bank as a whole, that is responsible for producing integrated information and that contains reports on the results of operations by the Regional Departments. This imposes some degree of difficulty in applying internal controls for project implementation supervision system.

2.11 The situation described above introduces significant transactional costs when it comes to using the information for other purposes. The information system as it stands, although it has evolved appreciably, does not satisfy one of the basic principles of the SEP design (see CP-1283), namely that the system of supervision "must be cost-efficient and must include only project-level information that is useful, readily available (throughout the project cycle), and simple, and can be incorporated into the Bank's database for easy updating and report production."

2.12 Delays in project execution also have a significant impact on supervision, imposing additional transactional costs to project execution and monitoring (see Annex B).

2.13 These time overruns are associated with a greater likelihood of circumstances that lead to nonfulfillment of the project's original objectives, thus reducing the net present value of its benefits and occasioning greater costs to the country. These overruns involve an opportunity cost for funds that could be used for other purposes, they increase the impact of risks in the project cycle, they expose more projects to the uncertainties of the domestic political cycle, they add to the likelihood of shifting priorities, they raise the possibility of project reformulation or cancellation, and they reduce the present value of the project's net benefits.[17]

2.14 This context also requires expanding periodic supervision activities beyond those planned, either to extend the deadline itself, or to deal with the greater risks implied. This raises supervision costs, adds to the financial costs of operations (fees and interest), and increases annual amortization installments, owing to a shorter loan repayment period.[18]

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[17] Similar concerns are indicated in document GN-2215-1, "Portfolio Management Action Plan", 6 February 2003, paragraphs 2.06 and 2.07.

[18] As of 2003, execution delays will not trigger automatic extensions in the project grace period, in which case countries may find themselves starting to repay the loan principal before the project's benefits have been realized.

III. THE DEGREE OF COMPLIANCE IN SUPERVISION ACTIVITIES

A. Measuring the degree of compliance

3.1 The instruments available in the Bank's supervision system are described in Annex A. This Chapter evaluates the extent to which that system operates in accordance with the supervision procedures established in Bank policies and regulations.

3.2 There are three key characteristics of the instruments that must be taken into account for purposes of this analysis. First, while supervision is a functional responsibility of the Regional Departments, primary responsibility for each tool rests with a different area (REs, COs, and other departments at Headquarters). Second, these instruments are of differing periodicities: some are performed periodically, normally on an annual basis, others only once in any stage of the project cycle, and still others aperiodically.

3.3 Third, not all instruments set out in Bank policies and procedures are compulsory. The regulations establish two levels of enforcement: instruments that are compulsory because they are established in Bank policies, and those are mandatory if specified in the project contract (BEP for example) or planned during execution (IVF for example). This is not to say that supervision activities not called for in Bank policies or during planning do not exist, but these will be examined elsewhere.[19]

3.4 These regulated activities establish a "minimum level" of supervision activities that are mandatory, as well as an "expanded level", if mandatory activities established in project contracts, or during the planning state are considered. The present study examines the degree of compliance at each level.

3.5 To measure the compliance of supervision activities, a Completeness Monitoring Index was established to convert the minimum mandatory supervision instruments to a Compliance Matrix set up as a binary system of zeros (if mandatory and not performed) and ones (if mandatory and performed). These are then averaged to produce the index. The closer the index is to one, the greater the degree of compliance with the minimum established for such activities.

3.6 The differing periodicities of the instruments called for consideration of two types of indices: a Completeness Monitoring Index (CMI) to measure compliance for mandatory periodic instruments (annually) that permits analysis of the present situation and trends for purposes of measuring progress; and an Overall

[19] Another indicator will be defined below, the "Effective Coverage of Supervision", which measures, ex-post, the relative importance of all supervision activities actually conducted by the Bank, compulsory or voluntary, against all activities that might potentially have been conducted during the period of analysis.

Completeness Monitoring Index (OCMI) to measure the degree of compliance for all supervision instruments, periodic or not. This latter index can only determine the degree of compliance for the entire 1998-2001 period.

Table 3
Monitoring Completeness Indices (CMI)
Criteria for definition

Monitoring instruments	Acronym	Responsibility center	Periodicity	Compulsory by	CMI (annual)	OCMI (1998-2001	Comments
Loan administration missions							
1. Start-up mission	MS	RE	One time	Project		*	
2. Annual review mission	MA	RE	Annual	Project	*	*	
3. Specific mission	MSP	RE	Occasional	Project			Combined with MAs
4. Midterm review mission	MMT	RE	One time	Project		*	
Portfolio review missions							
5. Annual country portfolio review mission	CPR	RE	Annual	Policy	*	*	
6. Sector portfolio review mission	SRM	RE	Occasional	RE&CO regs			Not considered in study
7. Annual portfolio evaluation	APE	CO	Annual	Policy			Not considered in study
Country Office instruments							
8. Technical inspection visits	IVT	CO	Annual	Policy	*	*	
9. Financial inspection visits	IVF	CO	Occasional	Policy	*	*	Mandatory if planned
10. External audit	EFA	CO	Annual	Policy	*	*	
11. Project performance monitoring report	PPMR	CO	Semi-annual	Policy	*	*	
12. Project completion report	PCR	CO	One time	Policy		*	
13. Borrower ex post evaluation	BEP	CO	One time	Project		*	
14. Bank final evaluation	FIN	CO	One time	Project		*	
Functions assigned to HQ departments							
15. Project alert identification system	PAIS	ROS	Ongoing	Function			Not considered in study
16. Operational/administrative review of COs	OR-AUG	AUG	Two years	Function			Not considered in study

3.7 In constructing the matrix databases, particular attention was paid to introducing temporary restrictions for each supervision tool in order to reflect their use over the period selected. These restrictions are indicative of the fact that the periods or times for which compliance applies varies from tool to tool. In some cases, this made it possible to standardize the criteria used for a given tool. As well, specific temporary restrictions were introduced so that the test would consider only project supervision activities that were supposed to be completed in the period 1998-2001. For example, in the case of the PCRs, the degree of compliance was measured only for projects with a last disbursement date falling after 1 January 1998 and before 30 September 2001. So, how each tool is applied depends on the nature of the tool itself and where it fits into the execution cycle.[20]

[20] These aspects may be consulted in greater detail in the electronic databases prepared for the study.

Box 1. Temporal restriction criteria used for the evaluation

Tool	Timing		Comments
	Initial	Final	
MS	DoE > 1 Jan 1998	DoE < 31 Dec 2001	Required by project and RE info
MA	DoE < 30 June t	CDD > 30 June t	Required by project and RE info
MSP	…	…	
MMT	DoE > 1 Jan t	CDD < 31 Dec 2001	>= 50% of disbursements and of time elapsed; required by project and info
SRM	…	…	
CPR	DoA < 30 June t	CDD > 30 June t	Presented and recorded at the Programming Committee (SEC)
IVT	DoE < 30 June t	CDD > 30 June t	RE info
IVF	DoE < 30 June t	CDD > 30 June t	RE info
PPMR			
June	DoA < 30 June t	CDD > 1 Jan t	
December	DoA < 30 Dec t	CDD > 30 June t	
PCR		CDD <=30 Sep 2001	
APE	...	…	LMS
BEP			CO; considering waivers and contract
FIN			CO; considering waivers and contract
EFA	DoE < 1 Jan t+1	CDD > 1 Jan t	LMS, if no waiver from CO
PAIS	…	…	Idem PPMR
OR-AUG	…	…	Administrative and operational review reports from Country Offices

Notes:
DoA = date of approval
DoE = date of eligibility
CDD = date of final disbursement
t = represents each year in the period considered
…= not considered in the database for analyzing the degree of compliance

B. The degree of supervision compliance: principal findings

3.8 This section presents the main findings of the empirical work on supervision activities conducted by the Operations Departments with the loan portfolio in execution during 1998-2001.

Table 7

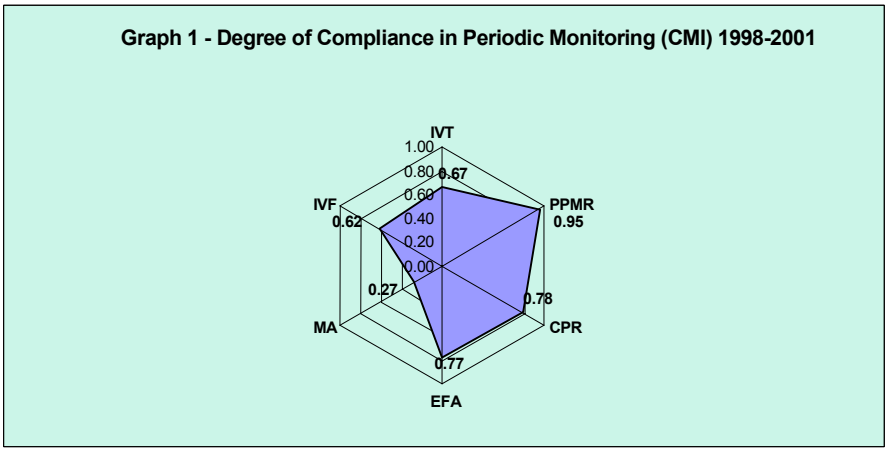
Degree of Monitoring Compliance, 1998-2001 - Periodic Completion Indices (CMI), by individual monitoring tool and overall (OCMI)

Year	Monitoring tools										CMI	OCMI		
	Compulsory by policy					Programmed by project and planned						Total	Compulsory	Programmed
	IVT	PPMR	CPR	EFA	PCR	MS	MA	MMT	IVF	FIN/BEP				
1998	0.64	0.97	0.79	0.77	…	…	0.27	…	0.60	…	0.78	…	…	…
1999	0.64	0.91	0.62	0.78	…	…	0.31	…	0.56	…	0.72	…	…	…
2000	0.65	0.94	0.85	0.78	…	…	0.32	…	0.76	…	0.79	…	…	…
2001	0.75	0.97	0.85	0.76	…	…	0.20	…	0.57	…	0.79	…	…	…
											0.77			
1998-2001	0.67	0.95	0.78	0.77	0.91	0.18	0.27	0.10	0.62	0.38		0.75	0.84	0.43

3.9 Table 7 shows aggregate findings for the Bank as a whole based on the different compliance indicators identified, and taking into account the differences in the periodicity and the compulsory nature of the supervision instruments.

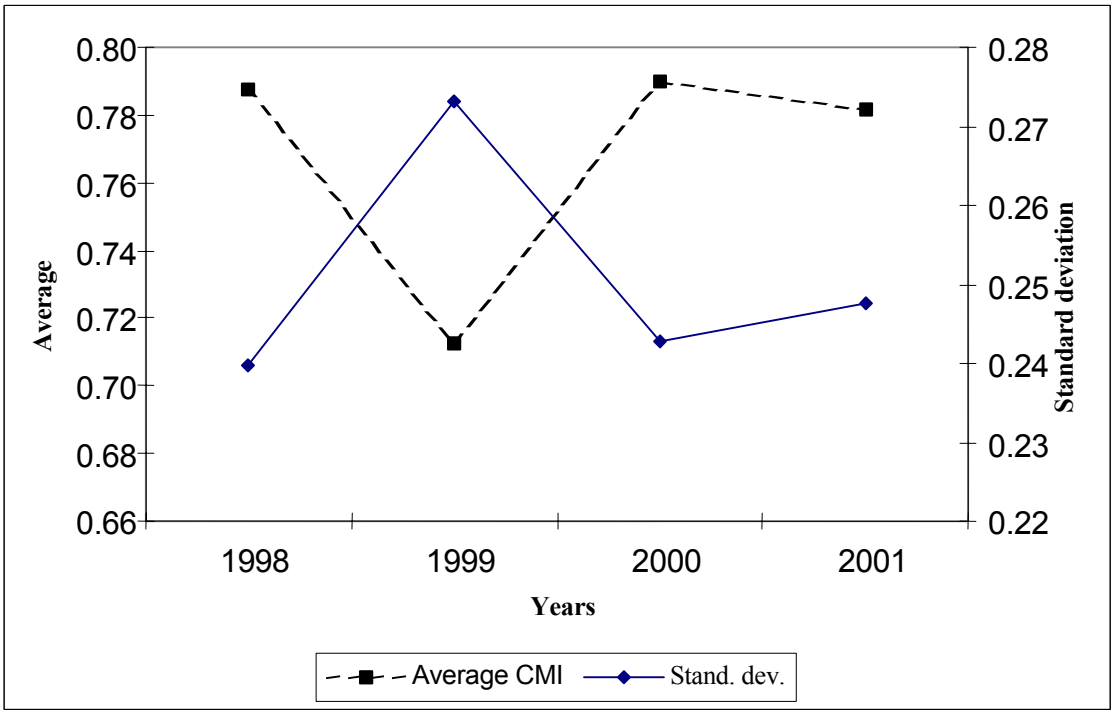
1. Periodic monitoring (CMI)

3.10 The CMI expresses the aggregate behavior of six supervision instruments: MA, IVT, IVF, PPMR, EFA, and CPR. These measures indicate that the Bank effectively conducts only 77% of the compulsory reviews and missions set out in institutional policies and project planning. Only the PPMR achieves average values close to 100%, while other instruments fall from 22% to 33% below the minimum prescribed levels, with the exception of the MA, where the figure exceeds 70%, and the IVF, where it is approximately 40%.



3.11 This indicator makes it possible to examine trends over time. There is a pronounced decline in the index for 1999, which then returns to its 1998 levels in the next two years, without however producing any substantive improvement in the average degree of compliance for the period as a whole. Nor is there any significant change in the magnitude and volatility of the results, expressed by the standard deviation of individual project results.

Graph 2 - Average CMI trend and standard deviation, 1998-2001



3.12 At the regional level, the CMI shows a higher minimum level in Region 1 (0.85) compared to Region 2 (0.72) and Region 3 (0.74). At the country level, using the results from a four-year transitional matrix, calculated between the years 1998 and 2001, it is found, first, that of 26 borrowing countries in 1998, 12 had a CMI above the Bank average; in 2001, the figure was 13. Second, of the 12 countries that were above the Bank average in 1998, two fell below that average in 2001 (GY and TT); of the 14 countries that were below the average in 1998, three improved their position in 2001, with results above the average (PR, BL, and CR). There were 11 countries that remained below the average in both years (CH, DR, HA, HO, ME, NI, BA, BH, JA, PE, and SU). The remaining countries were always above the average.

Table 5
CMI: Transition Matrix, 1998 and 2001

		2001	
		>= Bank CMI	**< Bank CMI**
1998	>= Bank CMI	83.3% **10 countries** AR GU BO PN BR CO UR EC ED VE	16.7% **2 countries** GY TT
	< Bank CMI	21.4% **3 countries** PR BL CR	78.6% **11 countries** CH BA DR BH HA JA HO PE ME SU NI

3.13 The degree of compliance in supervision activity, measured by the CMI, can also be appreciated by project type and by sector of activity.

Table 6
Degree of periodic monitoring compliance (CMI) by type of project

Type of project	Quantity	Amount (US$ mill.)	CMI				
			1998/2001	1998	1999	2000	2001
PSCT	47	7,302	**0.53**	0.56	0.44	0.50	0.58
PCTR	61	705	**0.77**	0.76	0.69	0.80	0.80
PESP	397	31,887	**0.80**	0.81	0.74	0.82	0.81
PGOM	52	5,023	**0.78**	0.80	0.76	0.79	0.77
PGCR	28	4,612	**0.74**	0.77	0.74	0.74	0.71
PHIB	7	1,168	**0.65**	0.68	0.64	0.68	0.60
PINO	11	90	**0.86**	…	…	0.78	0.89
PPFM	11	1,084	**0.79**	…	…	0.40	0.91
PSEF	2	9	**0.67**	…	….	….	0.67
Total	616	51,880	**0.77**	0.78	0.72	0.79	0.79

Table 7
Degree of periodic monitoring compliance (CMI) by sector of activity

Sector of activity	Quantity	Amount (US$ mill.)	CMI				
			1998/2001	1998	1999	2000	2001
RM	133	10,290	**0.71**	0.72	0.63	0.74	0.75
TR	64	6,952	**0.79**	0.81	0.76	0.81	0.80
IS	83	5,614	**0.77**	0.81	0.70	0.81	0.76
OS	52	5,367	**0.82**	0.80	0.80	0.87	0.80
DU	48	5,280	**0.80**	0.82	0.77	0.81	0.81
ED	51	4,078	**0.80**	0.80	0.74	0.78	0.85
EN	23	2,890	**0.77**	0.80	0.75	0.83	0.72
IN	7	2,815	**0.82**	1.00	0.79	0.88	0.77
AG	51	2,633	**0.74**	0.76	0.70	0.73	0.76
SA	27	1,853	**0.76**	0.72	0.70	0.77	0.82
PA	32	1,343	**0.79**	0.76	0.74	0.79	0.84
CT	14	940	**0.88**	1.00	1.00	1.00	0.69
MU	5	703	**0.62**	0.65	0.67	0.56	0.59
TU	8	625	**0.87**	0.83	0.93	0.89	0.83
ME	8	274	**0.72**	0.73	0.67	0.78	0.73
FO	4	133	**0.79**	0.88	0.62	0.86	0.78
PR	6	90	**0.83**	0.87	0.79	0.90	0.75
Total	616	51,880	**0.77**	0.78	0.72	0.79	0.79

3.14 By project type, the results show low CMI levels for PBLs (PSCT) and hybrid operations (PHIB) that combine investment with conditions. These operations exhibit a behavior distinct from investment loans, which have CMI scores of around 0.80. By sector of activity, there is a gap of nearly 30% in the degree of compliance in periodic supervision activities for transactions involving reform and modernization of the State, which account for most of the PBLs approved.

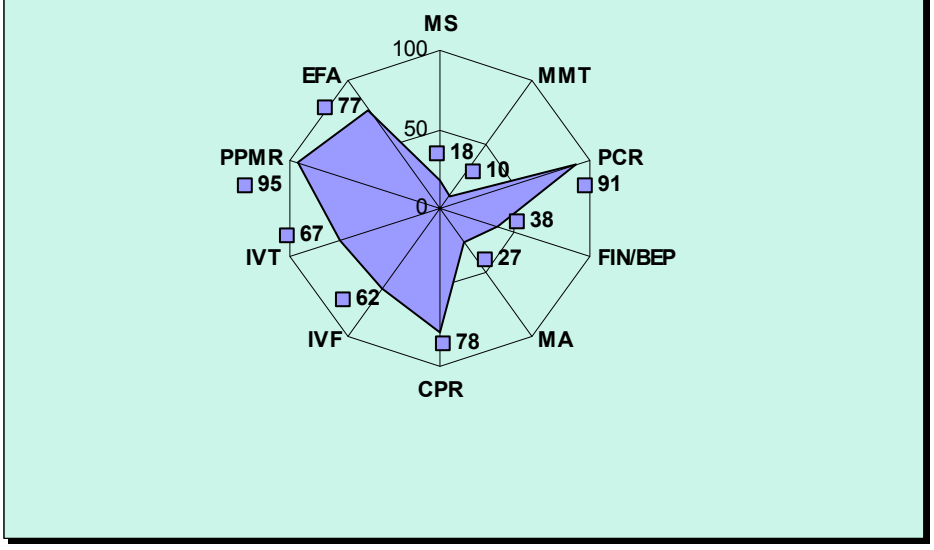
3.15 In conclusion, performance fell significantly short of the expected value by close to 1 for the CMI, and for each of its component instruments. The only compulsory

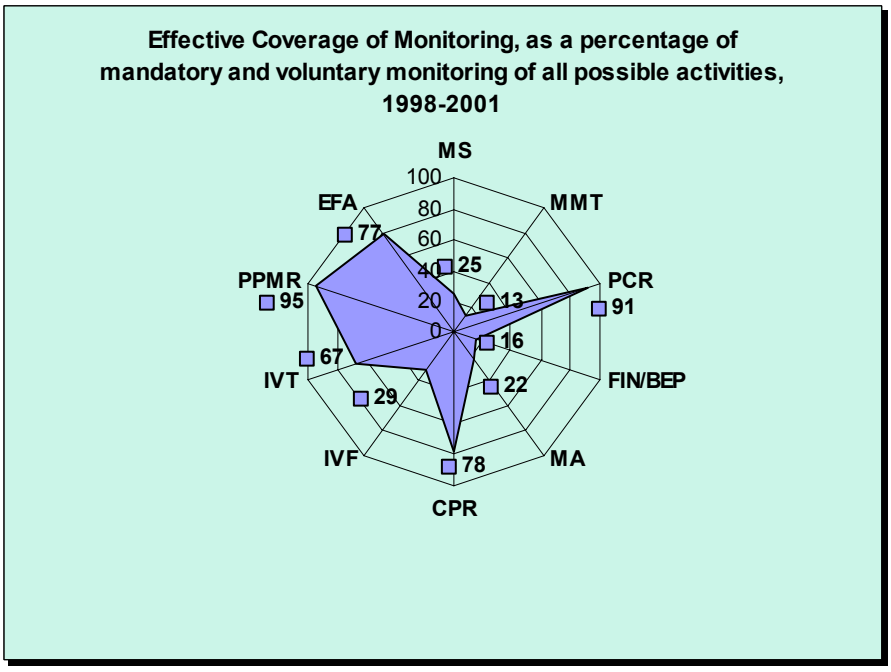
periodic supervision activity that achieves high compliance levels is the PPMR (95%), which seems to be the Bank's typical monitoring tool, regardless of region, country, project type, or sector.

2. Overall supervision (OCMI)

3.16 The OCMI is an indicator of the degree of compliance for all the minimum compulsory supervision instruments used by the Bank. In addition to the annual instruments in the CMI, the indicator includes four aperiodic instruments: MS, MMT, PCR, and FIN/BEP (which combine subsequent evaluations planned by Management or by the borrower). Because of the way it is constructed, the OCMI is able to reflect only the results for the period 1998-2001. The value obtained (0.75) is lower than that achieved by the CMI. Aggregating all the instruments does not result, then, in any improvement in the overall compliance of Bank supervision.

Graph 3
Overall Project Monitoring Compliance Indicators





3.17 Of the instruments being added, on average the compliance rating for the PCR was close to unity (0.91) compared with the low rating for the MS (0.18). The noncompliance gap for the MMT is at around 90%, and for the FIN/BEP the gap between supervision executed and planned was also very low, exceeding 60%.

3.18 If supervision instruments are grouped according to whether they are compulsory under Bank policy or mandatory because they are planned as part of a project, the outcome indicates that the degree of supervision compliance in the first group ("minimum compulsory level") is 0.84, while the figure for project-stipulated supervision is only 0.43.

3.19 In the period 1998-2001, the relative importance of mandatory supervision activities called for in projects was low (31%), ranging from 5% for MS to 49% for FIN/BEP. The IVTs were planned for 45% of eligible projects, while the figure for MAs was 18%, and for MMTs 33%. When these results are adjusted for degree of compliance with programmed activities, the relative importance of project-stipulated supervision is even lower (15%).

Table 8
The importance of project-stipulated monitoring activities

Period	No. of monitoring activities stipulated or planned in projects					Total
	MS	MA	MMT	IVF	FIN/BEP[1]	
1998-2001	29	244	202	619	303	
Representativeness (%)	5.1	17.6	32.8	44.6	49.2	31

[1] 153 projects called for FIN and 149 for BEP, excluding waivers.

Note: The degree of representativeness of MS was calculated for projects in execution, excluding the PSCT; for MA and IVF, the figure reflects those planned in all eligible projects in execution; for MMT and FIN/BEP, all projects in execution during the period.

3.20 Another way of looking at compliance in supervision activities is the "Effective Coverage of Supervision" (Graph 5). This ex post indicator measures the relative importance of all supervision activities conducted by the Bank, both mandatory ones and voluntary ones not stipulated in project contracts, against the total of all possible supervision activities that might have been conducted in 1998-2001 with each tool.

3.21 This indicator reveals two special features of supervision instruments that are programmed for projects. First, there has been an increase in supervision not called for in projects (primarily MS and MMT). The MS end up covering 25% of possible projects (those initiated in 1998-2001) compared to an OCMI of 18%. MMTs were conducted for 13% of possible projects during the period (compared to an OCMI of 10%).

3.22 Second, the change with FIN/BEP and IVF is rather similar but in the opposite direction. If the "planned-in-advance" restriction is removed, these instruments show no growth in voluntary activities to offset the coverage decline in the two indices. Their total coverage level stood at 16% and 29%, respectively, compared to OCMIs of 38% and 62%. These two instruments are used in supervision of

development and financial risks, respectively. Both aspects are considered later in this report.

3.23 In conclusion, it will be noted that, first, the comprehensive measurement of supervision instruments using the OCMI (0.75) does not improve compliance performance with periodic instruments, as measured by the CMI (0.77). Only two of the supervision instruments produce figures close to unity: these are the PPMR and the PCR, which would seem to be the typical instruments with the greatest central monitoring in the Bank.[21] The programming of supervision activities called for in projects is very low (31%) for all projects in execution, and this figure is much lower still (15%) if the sample is restricted to programmed supervision activities actually completed.

3.24 This indicates that planned supervision activities (MS, MA, MMT, IVF, FIN, and BEP) other than the "compulsory minimum level" established in Bank regulations is barely used in project designs. When supervision activities either not anticipated or programmed into projects are considered, the coverage of MS and MMT improves slightly, while the coverage of other project-planned instruments declines.

3. The sequencing of supervision activities

3.25 The various supervision instruments used by the Bank have a logical sequencing that revolves around the PPMR, which appears to be the pivotal tool for the entire system. The basic inputs that go into the PPMR are the project design, together with the results of the start-up mission (MS) and the inspection visits conducted during implementation. Under Bank regulations, the PPMR is in turn used as basic input for other supervision instruments, particularly the CPR, the terms of reference for all LAMs, the annual APE, the PAIS alert system, the PCR, and the FIN/BEP.

3.26 Consequently, in analyzing the logical sequencing of supervision activities, it is reasonable to expect that the input-output ratio can be tested, as a way of assessing the functional health of the SEP. A positive result would be one in which each supervision output in that sequence would have a similar proportional probability of occurring, close to 100%. The main empirical findings[22] on this point are as follows:

a. MS were planned for 5% of projects that began execution in 1998-2001, and 25% of that total were actually performed, considering programmed and unprogrammed execution.

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[21] Although the CMI for the PCR is 0.91, this figure does not reflect the fact that in 2001 only 67% of PCRs were approved within policy-mandated time limits, and this figure is even lower in 2002 (41%). Source: document GN-2215-1.

[22] The evaluation databases were constructed by year, imputing to each project in the sample the totality of supervision outputs produced in each one. This allowed for testing the input-output correspondence between supervision activities that are planned as part of the same process.

b. IVTs were conducted, on average, for only 67% of projects in execution that had a PPMR.
c. IVFs were planned on the basis of risks for 45% of all projects in execution, and effectively carried out for 29% of that percentage, taking into account planned and unplanned activities.
d. 95% of projects in execution during the period had their two PPMRs per year.
e. Only 78% of projects that had a PPMR were considered in country CPRs. The lower compliance figure for CPRs, besides denying the opportunity to discuss execution problems with the countries, meant that the work that went into preparation of the PPMR's was not used for that purpose.[23]
f. The compliance rate for the PPMR (95%) made these important inputs for other outputs (PCR, APE and PAIS, primarily).
g. Given the low proportion of FIN/BEP performed within the total of executable projects in the period (16%), most projects failed to benefit from the lessons of an independent final evaluation.

3.27 To conclude, the approach to project supervision suggests the following. First, while the use of MS has not been significant (25%) as an input to project implementation and monitoring, this percentage is even lower when only those MS called for in project design (5%) are considered.[24]

3.28 Second, in a significant number of projects, the preparation of the PPMR is not based on prior inspection visits. While PPMRs were performed in 95% of projects in execution, IVTs were conducted for only 67%, and IVFs were planned as a function of risk for only 45%, and were executed for only 29%, of planned and non-stipulated activities.

3.29 Third, a considerable number of projects with semiannual PPMRs (22%) were not reviewed by the Regional Manager or Deputy Manager and the government authorities to resolve problems because the respective CPRs were not conducted.

3.30 Finally, the quality of project outcomes is determined fundamentally by the outputs of self-evaluation (PPMR and PCR), in which there is very little participation by beneficiaries.

4. The use of supervision instruments linked to performance evaluation and dialogue with the borrowers

3.31 Annex C analyzes the use of supervision in portfolio performance evaluation as well as in the results of dialogue with borrowers.

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[13] "CPRs conducted" refers to those that were presented and discussed in the Programming Committee.

[24] This activity is essential for informing borrowers and the COs about relevant aspects of operations, monitoring parameters and activities, and the objectives of the operation.

3.32 The first group of instruments are employed relatively little for supervision of performance evaluation except in the case of self-evaluation. In fact, such instruments (MS, MMT, FIN, and BEP) are programmed for one third of projects, yet only 15% of the activities planned are actually conducted. The performance of MS is better than programmed, but starts from a very low base. The MMTs, which are used for monitoring the results during execution, are important because of their capacity to pinpoint potential problems in advance. They are actually performed, though, in only 13% of possible cases. The Bank supervises the evaluation of results, using mainly self-evaluation instruments, such as the PPMR and PCR, in which participation by borrowers and beneficiaries is either not provided for, or is voluntary.

3.33 Supervision of the dialogue with the borrower has been on the rise, with participation by the borrowing member countries, but the levels attained so far are still well below potential and limited mainly to CPRs. This tool is the main periodic institutional mechanism of dialogue for addressing risks to project objectives. Considering also that executing agency participation in the PCR is voluntary (there is no information available to indicate the degree and type of actual participation by beneficiaries in the process), the effective level of borrower involvement may be even less.

IV. SUPERVISION OF PROJECT FIDUCIARY RISKS

4.1 The Bank's risk supervision focuses primarily on two broad areas: first, the appropriate use of project funds, and second, the achievement of development objectives.

4.2 This chapter evaluates supervision of funds administration, and the capacities of executing agencies to administer resources, the functioning of the systems for administration and control of Bank funds, and the handling of ethical risks.

4.3 The fiduciary supervision instruments used by the Bank are primarily the annual independent external audits (EFA), the financial inspection visits (IVF), and the administrative and operational reviews of the Country Offices that are performed every two years by the Auditor General's Office (OR-AUG).

A. External Financial Audits (EFA)

4.4 Once a loan is eligible for disbursement, an independent annual audit of its financial statements is required. The audit is commissioned by the borrower, and compliance is reviewed by the CO and confirmed by the Audit Division (DAU) of ROS.[25]

4.5 External auditors issue their opinion annually using a normal system with various qualifications that are, however, recorded in the LMS in binary notation: EFA with observations (qualified) and EFA without observations (unqualified), reflecting "clean" audit opinions.[26] [27] Moreover, as a result of its review of external audit reports and opinions, the CO may issue an opinion of its own as to whether the findings on which the EFA reservations are based will affect project execution.[28]

4.6 The office responsible for monitoring audit quality is ROS/DAU, which it does on the basis of a sample of loans and countries taking the opinions into account. On the basis of its analysis, it produces an internal memorandum on the issues and sets out various courses of action depending on the problem, for incorporation into the CO plans. It reports missing or late EFAs, but makes no attempt to assess the risk relating to their quality.

4.7 Existing regulations require that an EFA be classified as "qualified" if there is any adverse opinion about the financial statements. As far as could be determined, there is no provision in Bank policies for the CO to express reservations on the external auditors' opinion. Consequently, the risk relating to the proper recording of loan funds management is identified by the Bank with the classification "qualified". This classification assigns excessive responsibility to problems in the handling of funds

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[25] On this point, the universe of analysis is taken as loans, rather than projects, since it is to loans that the EFA applies. Quick-disbursing loans (PBL and emergency loans) do not require an EFA, although the Bank reserves the right to insist on one. As soon as the loan is eligible, an audit will be conducted, and it will be determined whether the executing agency is to be audited. Where loans involve financing from two sources, (i.e. OC and FSO), only one audit is required. If loans contain various subprograms, these will be treated as subloans and there will be several audits. DAU/ROS records the identity of the auditor for each loan; whether the executing entity is also to be audited; the contract period and any extension if it has expired; the contractual date for original acceptance of the audit; the date of receipt in ROS, which reports on audits not received; the date of approval of the qualification by the CO; whether waivers of the EFA requirement have been issued for a given period; classification of the auditor's opinion (Q = qualified, U = unqualified); and any reservations by the CO as to execution problems encountered in its review, by means of an entry of Y (yes) or N (no), confirming whether or not the auditor's observations affect project execution.

[26] The LMS records as "Q" (qualified) any external audit opinion that contains observations or reservations, or an adverse opinion, or refrains from comment because of limitations in scope, while U (unqualified) is reserved for an opinion that is "clean."

[27] Beginning in August 2003, the binary classification regarding the opinion of the independent auditors included in the LMS was changed to reflect four types of opinions: clean, qualified, adverse, and denial of opinion.

[28] These reservations of the CO to the external auditors' reports may refer to such issues as: formal legal and taxation aspects, labor legislation, financial and accounting aspects, limitations to the scope of work, etc.

and financial statements, since any opinion that is not "clean" is regarded as having reservations.

4.8 The reservations that a CO issues on the ROS binary classification should be construed as an assessment of the magnitude of the problems affecting project execution. This does not mean, however, that the risks relating to loans with EFAs classified as "qualified" and reported "No" by the CO are considered irrelevant by ROS.

4.9 Following is a presentation of results on the degree of compliance of the EFAs, in light of Bank policies and funds management performance, together with a measurement of the risk level revealed by their classifications. Both aspects are measured, taking into account their volume based on the number of loans and annual disbursements. The results are also presented in light of the opinions issued by the external auditors, as well as the reservations expressed by the COs on those opinions.[29]

Table 9. Performance of External Financial Audits (EFAs)

Year	No. of loans eligible for EFA after waivers	No. of loans without EFA	No. of loans with EFA, classed with observations	No. of loans with EFA classed without observations	Degree of compliance of EFAs	Degree of confidence in use of funds	Amount of disbursements without EFA (US$ millions)	Amount of disbursements with EFA, classed with observations (US$ millions)	Amount of disbursements with EFA classed without observations (US$ millions)	Total disbursements (US$ millions)	Degree of compliance of EFAs	Degree of confidence in use of funds
	1	2	3	4	5= (1-2)/1	6 = 4/1	7	8	9	10	11= (10-7)/10	12 = 9/10
					EFA results							
1998	451	104	151	196	76.9	43.5	656	2,263	1,778	4,697	86.0	37.9
1999	520	121	125	274	76.7	52.7	457	1,294	2,532	4,282	89.3	59.1
2000	547	128	147	272	76.6	49.7	948	976	2,177	4,101	76.9	53.1
2001	570	156	116	298	72.6	52.3	1,468	764	2,928	5,160	71.5	56.7
Average	522	127	135	260	75.6	49.8	882	1,324	2,354	4,560	80.6	51.6
					EFA results adjusted for CO opinion							
1998	451	104	68	279	76.9	61.9	656	570	3,471	4,697	86.0	73.9
1999	520	121	68	331	76.7	63.7	457	698	3,127	4,282	89.3	73.0
2000	547	128	67	352	76.6	64.4	948	517	2,635	4,101	76.9	64.3
2001	570	156	72	342	72.6	60.0	1,468	555	3,137	5,160	71.5	60.8
Average	522	127	69	326	75.6	62.5	882	585	3,092	4,560	80.6	67.8

4.10 As to compliance, it will be noted that EFAs were performed for only 76% of eligible loans, excluding waivers authorized by the COs. This figure rises to 81% when considering amounts disbursed subject to audit. The COs granted waivers in 37 cases during the period.

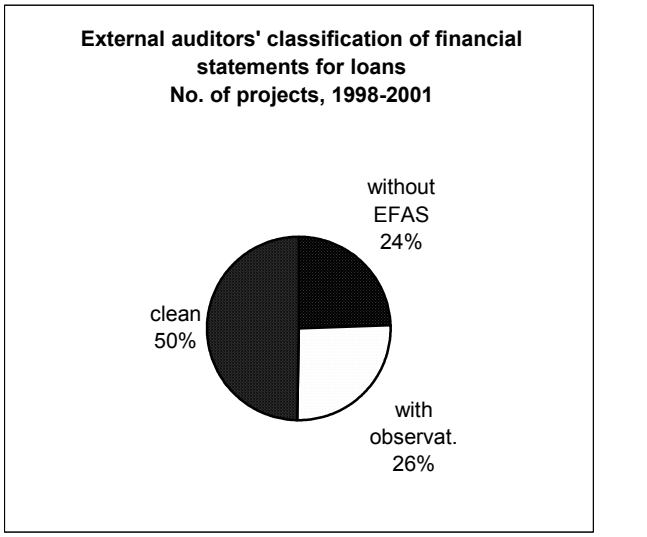
4.11 With respect to measuring risk, the study uses a confidence indicator defined as a function of the performance recorded in the EFAs. That indicator is the proportion of loans with EFAs without observations compared to total loans with EFAs, after waivers. In other words, less confidence is placed in loans with observations, and those where nothing is known because they are not backed by an EFA. The

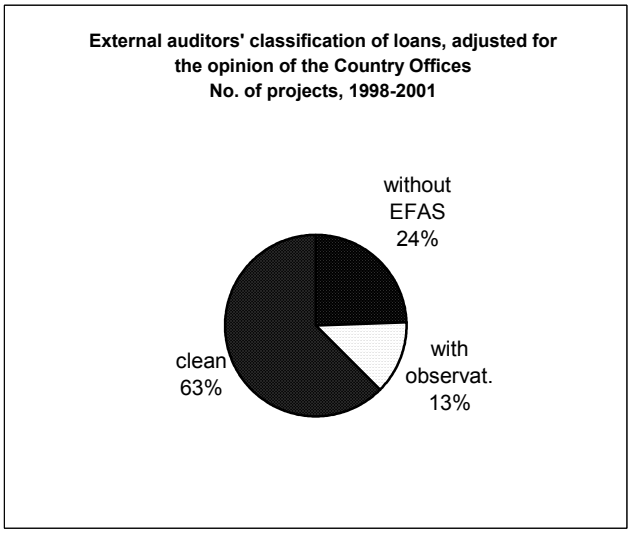
[29] The quantitative analysis was conducted using information from the LMS for March 2003.

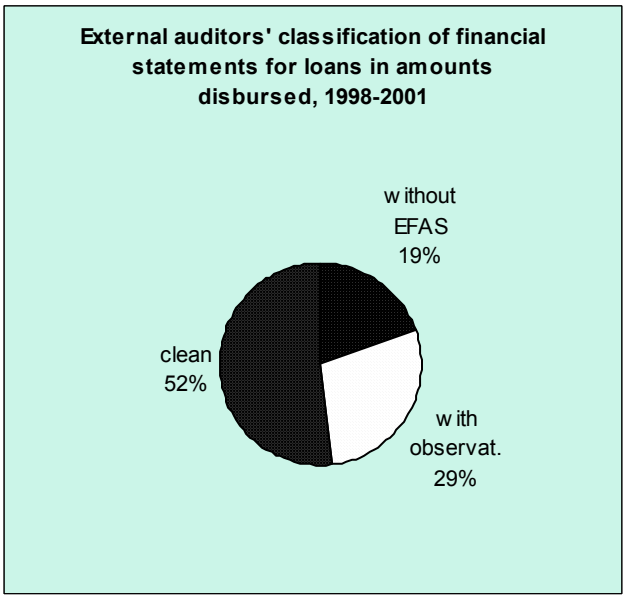
indicator is therefore an index of confidence, and not of certainty, as to whether resources have been used properly.

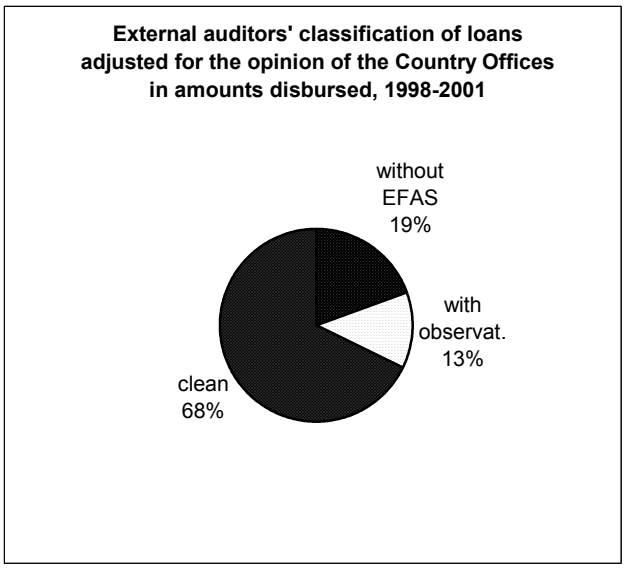
4.12 The confidence index for 1998-2001, based on EFA opinions, is 50% if measured by the number of loans, and 52% if calculated on the basis of disbursements. These figures rise to 63% and 68%, respectively, taking into account the opinions issued by the COs on the relevance of the problems encountered in the EFAs.

Graph 4









4.13 A highly significant conclusion, from the annual averages shown, is that for 50% of all loans that required EFAs in 1998-2001 (262 out of 522 loans), either the EFAs

were not performed (24%), or the EFAs were classified with observations by ROS (26%). Following the same reasoning, but using average annual disbursements, 48% of all disbursements related to loans with some kind of confidence problem (US$2.206 billion out of US$4.560 billion on average), of which 19% related to loans that had no EFA, and 29% to loans with EFAs classified with observations. Considering the annual trend of the indicators, it will be seen that this risk situation increased over the period.

4.14 Looking at these calculations in the best light (i.e. as adjusted for the reservations expressed by the COs on the binary classification as defined in the LMS), the results are still significant, although more moderate. For 37% of loans requiring EFAs, either the EFA was not conducted (24%), or it contained some type of observation (13%). Considering average annual disbursements, 32% of amounts disbursed showed some kind of problem: 19% had no EFA, and 13% had an EFA with observations.

B. Financial inspection visits (IVF)

4.15 This tool was previously analyzed in relation to evaluating the degree of compliance with Bank regulations. This section examines the importance of its use as a supervision tool, and the extent to which IVFs were performed on the basis of funds management risk factors.

Table 10
The use of inspection visits as a tool for monitoring the use of project funds

Year	No. of projects with IVF	No. of projects in execution that could require IVF	Degree of use of IVF in monitoring (%)
	(1)	(2)	(3) = (1) / (2)
1998	68	309	22
1999	81	351	29
2000	121	361	56
2001	136	368	54

4.16 The information presented shows that financial inspection visits have become an increasingly important tool in the monitoring and evaluation of an executing agency's financial and accounting capacity. Coverage rose from 22% of projects that could have required IVFs in 1998 to more than 50% of projects by the end of the period. Consequently, Country Offices have been monitoring projects mainly through an examination of financial statements and EFAs, not through inspection visits.

4.17 The second aspect—the extent to which financial inspection visits were used for monitoring of projects identified as posing risks in the handling or use of funds—was addressed in the following manner. First, the universe of projects at financial

risk was defined as those with EFAs containing observations (projects without EFAs were excluded). Next, a subuniverse was constructed of projects with EFAs containing observations, but with reservations on those observations issued by the COs.

4.18 Of the total number of projects with EFAs containing observations, depending on the year, between 27% and 54% are recorded as having financial inspection visits. As a consequence of the CO's opinion of the ROS classifications, 71% of the financial statements of projects with EFAs containing observations were confirmed as having reservations.

Table 11
The use of financial inspection visits as a tool for monitoring risk in the use of funds

Year	No. of projects with EFAs containing observations	IVF for projects with observations		Use of financial monitoring in problem projects (%)	No. of projects with EFAs containing observations, with reservations by CO	No. of projects observed by CO with prior inspection visits (%)	No. of projects with observations after adjustment by CO	IVF for projects with observations		Use of financial monitoring in problem projects with adjusted classification (%)
		0 visits	>=1 visit					0 visits	>=1 visit	
	[1]	[2]	[3]	[4]=[3] / [1]	[5]	[6]	[7]	[8]	[9]	[10]=[9] / [7]
1998	135	94	41	30.4	103	39.8	32	28	4	12.5
1999	109	80	29	26.6	73	38.4	36	24	12	33.3
2000	124	68	56	45.2	93	60.2	31	20	11	35.5
2001	101	47	54	53.5	65	83.1	36	18	18	50.0

4.19 It will be seen that, in several cases, the opinion of the CO on the classification of the EFA was issued without a prior inspection visit: in 1998, only 40% of those opinions were preceded by an IVF. This figure rose to 83% in 2001, demonstrating an improvement in this aspect. As well, despite the reduction in the universe of projects at risk, after adjusting for reservations of the CO, the rate of financial inspection visits for projects with observations showed no improvement over the unadjusted situation: it rose from 13% of projects at risk in 1998 to 50% in 2001 (see column 10).

Table 12
The oversight response to identified financial risk
Dynamic analysis: transition matrices between two consecutive years
(as% of projects at risk in the preceding year)

Period	No. of projects at risk[1]	Degree of oversight response		
		No. of IVF planned	No. of IVF conducted	
			Planned	Planned and not
1998-1999	135	38%	25%	30%
1999-2000	109	46%	33%	40%
2000-2001	124	60%	44%	48%

[1] Classified with observations in the EFA

4.20 A dynamic analysis was performed to see how supervision through IVF responds to risks. The degree of supervision response was calculated by the percentage of IVFs

planned and effectively executed in the year following the one in which the project was identified as having EFA observations. It will be seen that planning in this category of projects was growing, but never exceeded 60%. Yet, if measured by planned IVFs actually performed, that maximum percentage falls to 44% of projects at risk. This figure rises to 48% when considering all IVFs executed, whether or not planned.

4.21 In conclusion, it is apparent that in the period under review, financial inspection visits were not the principal tool for supervision of the financial and accounting capacity of executing agencies. More important was supervision through the examination of financial statements and EFA reports. Also, monitoring of at-risk projects with IVFs, at best, did not exceed 50% of projects in that category. Lastly, considering the subset of projects at risk, there was relatively little monitoring of them by IVFs, particularly in terms of actions planned and effectively executed (44%).

4.22 All of this indicates that, to a significant degree, financial inspection visits were neither planned nor performed according to identified funds management risk.

C. Administrative and operational control by AUG

4.23 The AUG focuses its efforts on a review of how the instruments relating to Country Office operational and financial supervision are applied. The AUG is part of the Bank's system of control, not line agency controls which are the sole responsibility of the departments, acting as a supervision control. In this sense, the task of the AUG cannot be considered part of its internal controls insofar as it is not a regular control, but one that is used only to verify the efficiency and effectiveness of the Country Office operational and financial administration supervision process.

4.24 Based on the review of the documents OVE receives from the Auditor General's Office concerning the review of Country Office operational and administrative activities, two areas were examined: First, supervision instruments that are normally covered in an AUG opinion, and, second, classification of the most frequent recommendations found in reports (while respecting their confidentiality) that might point to common problems of supervision and the trend. The main findings are summed up in the table below:

Box 2
Frequency of AUG reviews of monitoring instruments and main recommendations 1998-2001

Oversight Tool	Frequency of reports with recommendations	Summary of most frequent recommendations
LAM	2	Improve mission coordination to avoid overloading the CO
IVT IVF	30 30	Improve the quality of reports Program visits on a realistic basis Organize work to comply with planning Introduce planning for monitoring and control Report visit results to the executing agencies Report to the region on the annual visits program Ensure that the visits program covers all projects Maintain updated files with the number and outcome of inspection visits Increase the frequency of inspection visits
PPMR	14	Ensure that financial information is integrated into the report Strengthen quality control to reflect the results of the latest actions and situations pending
PCR	14	Improve the preparation of reports by the established deadlines Improve the preparation of the PCR in accordance with the new procedures Involve the borrower in preparation of the PCR
EFA	34	Reduce delivery times Reduce review time Report in writing to the executing agency on compliance/noncompliance with financial clauses Updated information in the LMS
APE	5	This periodic practice of portfolio review, after updating the PPMR, is important
Oper. procedures review	37	Not considered in this evaluation

No. of AUG reports reviewed	37

Note: AUG reports do not include information on other monitoring instruments.

4.25 Since 1997, AUG has produced 37 documents covering the period 1998-2001, and the principal recommendations contained in those reports are summed up below. Using the frequency with which recommendations appear in the reports, it is evident that most by far address problems having to do with inspection visits and EFAs. There was no analysis nor were any specific recommendations made about the Bank's supervision system.

4.26 The most frequent recommendations on individual products indicate concern about the low proportion of technical and financial inspection visits planned and conducted as well as about the failure to plan inspections on the basis of each project's inherent risk. Also mentioned was concern about a frequent failure to report the results to both borrowers and Regional Operations Departments, and to maintain updated files. On several occasions, concerns were expressed about the quality of inspection visit reports, and about the frequent failure to integrate financial factors into the Bank's self-evaluation instruments (PPMR). With respect to the EFAs, consideration was often delayed as were file updates and the findings tend not to be reported. These recommendations are consistent with the findings on the use of these instruments contained in the present report.

V. SUPERVISION OF PROJECT DEVELOPMENT RISKS

5.1 This section evaluates supervision of the development risks that prevent a project's outcomes from being maximized to their full potential. The Bank uses two complementary assessment instruments (PPMR and PAIS) to identify the development risks it assumes with an operation (See Annex D: Supervision instruments for monitoring project execution development tisks).

A. Quantifying the development risk for the Bank's portfolio

5.2 This section provides a quantitative analysis of the level and performance of projects posing development risks, according to the systems established by the Bank. The analysis considers the number of projects in such situations, as well as their economic equivalent, measured by the value of the approved portfolio involved, and by their importance in terms of annual disbursements.

1. Number of projects on development risk alert

5.3 To measure the universes of projects at risk, given the heterogeneity of the systems used by the Bank, the portfolio in execution was divided into four categories. The first, consisting of projects on alert status as a result of PPMR classifications, includes projects with a DO classification of Probable or Highly Probable (DOB, where B indicates a classification of Buena [good], but where there are problems with the necessary conditions for implementation, IP classification of Somewhat unsatisfactory or Unsatisfactory (IPM, where M indicates Mala [bad]) and/or unfavorable sufficiency conditions in terms of progress, AS classification of low probability (ASM).

5.4 The second category, consisting of projects on alert status under the PAIS, adds to the previous universe those projects that, while classified as normal (DOB, IPB, and ASB) have two or more indicators of potential problems from the eight complementary parameters defined by ROS.

5.5 The third category is the same as the previous one, but includes projects from the at-risk sample determined by the PPMR classification that were not considered as projects on alert status in PAIS. The subset is known as "Adjusted PAIS", and is consistent with the ROS grouping only for the last year under consideration (2002).

5.6 The fourth and final category, known as "Total Risk" adds to projects on PAIS alert status the "Problem Projects" that are considered incapable of achieving their development objectives (classification Low Probability or Improbable, DOM), regardless of their IP or AS classifications. In fact, these projects are distinguished from those on alert status because they have a higher probability of failing to achieve their intended outcomes.

5.7 Nevertheless, the empirical analysis shows that problem projects change their classification significantly over time.[30] In 2001, 64% of projects that were in problem status in 1998 showed improvements in their DO-achievement classification, and 43% had become normal. As well, problem projects were not normally classified as such at the outset:[31] 53% of problem projects in 2002 had been classified as normal in 1998, and only 18% had been classified as problematic. This would suggest that only one-third of problem projects are likely to end up in problem status, and that of those only 20% were classified as problem projects at the outset.

5.8 From the information on the categories considered, a series of relevant trends can be extracted. First, the development risk in the number of projects in execution is significant and rising, in all subsets considered, and grew significantly in 2002.

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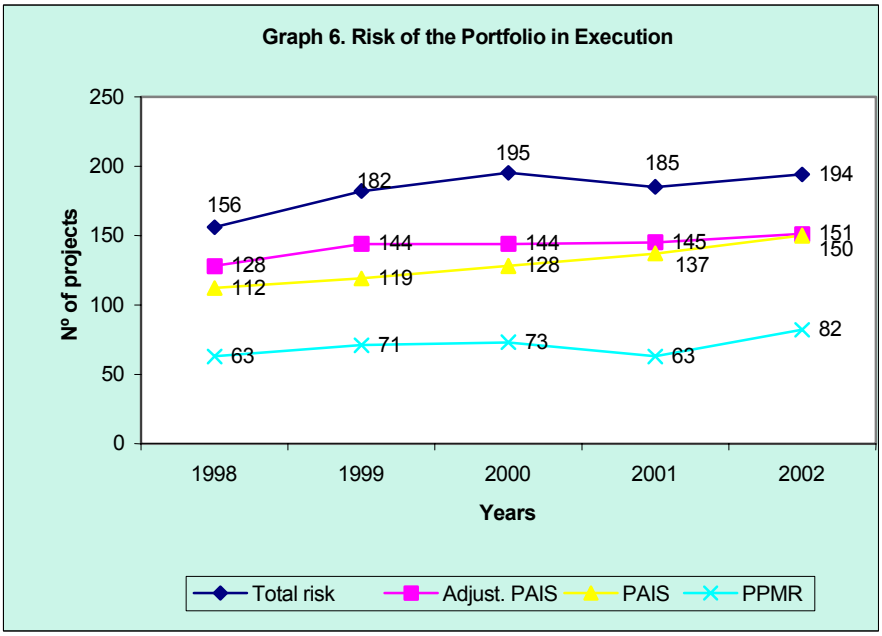
[30] Of those classified as problem projects in 1998, 36% retained that status in 2001, 21% were on PAIS alert, and 43% were normal.

[31] Of problem projects in 2002, 53% had been normal in 1998, while 29% had been on alert and 18% in problem status.



5.9 Second, the differences in the results of the two systems for evaluating development risk are significant and do not converge over time. The number of projects declared on alert by PAIS (30% to 35% of the total) is nearly double the number of projects on alert recognized in the PPMRs (13% to 19% of the total). The PAIS alert classification is not, for the most part, confirmed through classification changes by the Operations Departments, which are responsible for risk supervision and classification. This is an issue of growing concern to ROS and the Board of Executive Directors.[32]

5.10 Third, the projects on alert status plus the problem projects (Total Risk) have never accounted for less than 37% of the total portfolio in execution in any year, and reached 45% of the portfolio in 2002. Problem projects accounted for between 7% and 11% of the figure.

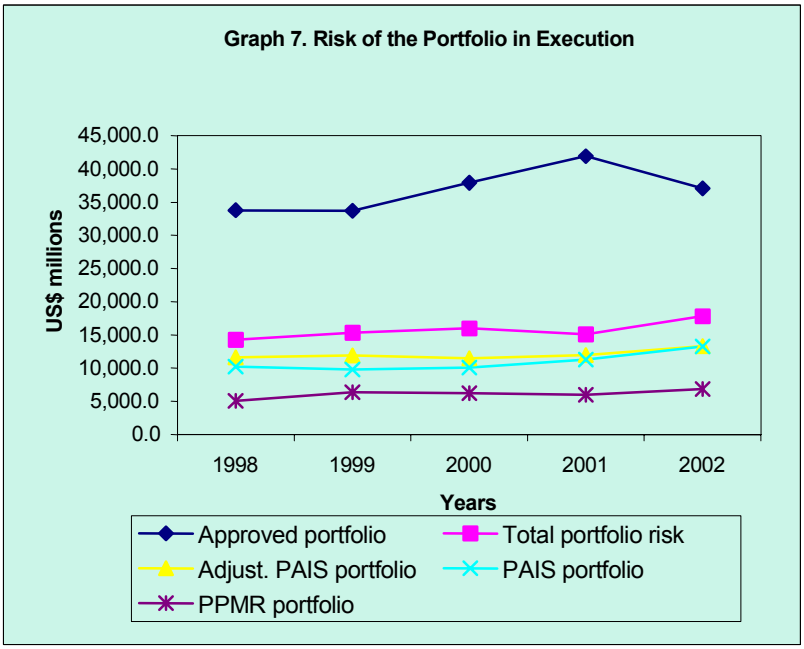
2. The economic significance of development risks

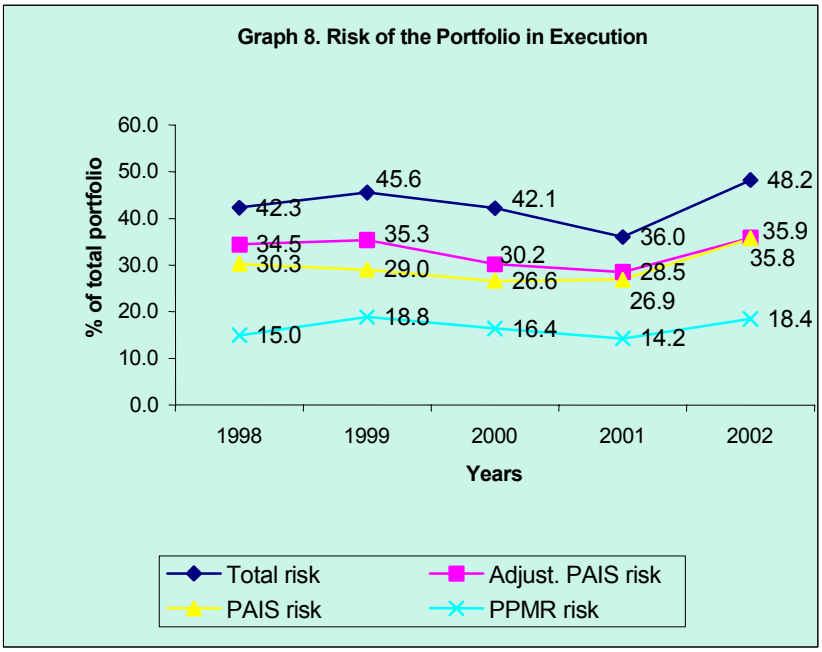
5.11 This section performs the same analysis, but instead of the number of projects it looks at the equivalent in the original amount approved for projects in execution in 1998-2002.

5.12 While the trends are similar to those noted above, there are some significant differences. First, as the value of the portfolio grew in 2000 and 2001, the risk as measured by the Bank's monitoring systems was high but declining. In 2002, there

[32] See document GN-2215-1.

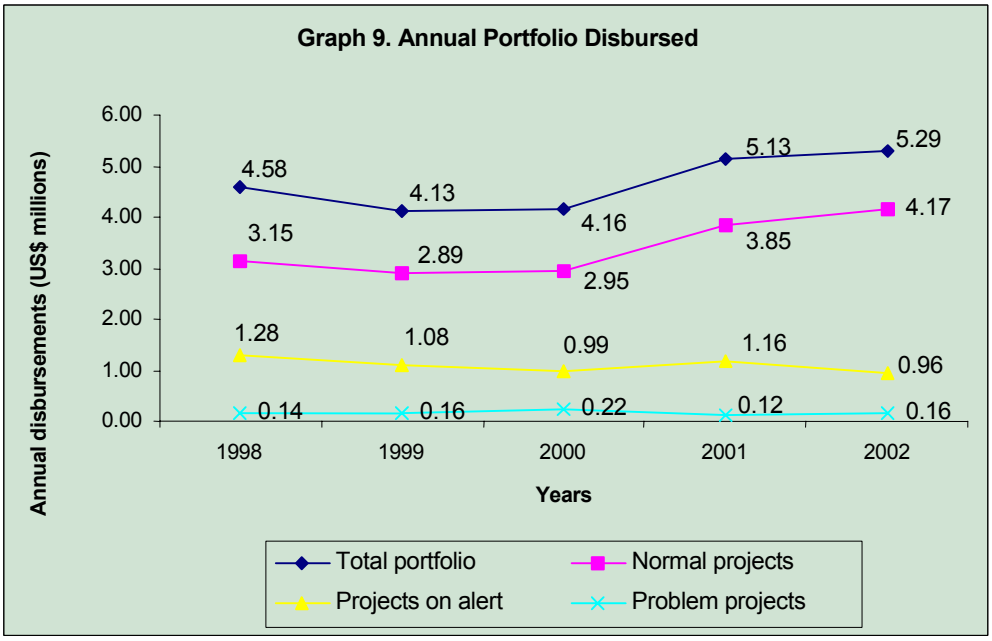
was a significant decline in the annual portfolio approved, producing a sharp increase in projects on PAIS alert and in problem status, although the change is less if only projects flagged in the PPMRs are considered.





5.13 Second, there is still a lack of convergence between the two systems for measuring projects at risk, and the discrepancy increases significantly in 2002. In that year, projects flagged by the PPMRs accounted for 18%, while those placed on alert by PAIS amounted to 36%, of the original approved portfolio in execution. If problem projects are factored in, 48% of the approved portfolio of projects in execution in 2002 was at some degree of risk in attaining their development objectives.

5.14 A similar analysis that considers annual amounts disbursed for the portfolio at risk shows that annual disbursements have been rising for the normal portfolio, particularly in the last two years (27%), but not for the portfolio at risk. With total disbursements expanding, then, disbursements for the portfolio at risk have remained relatively unchanged. While annual disbursements rose by 15% between 1998 and 2002, projects on PAIS status and problem projects together declined from 29% of disbursements in 1998 to 21% in 2002.



3. The internal distribution of the portfolio at development risk

5.15 According to the criteria for assigning classifications, not all portfolio combinations have the same probability of development risk. For example, from the risk viewpoint, a low probability of assumptions holding true has greater importance, because it is directly linked to sufficiency conditions for achievement of development objectives. For any two projects on alert status with an unsatisfactory IP classification, but divergent assumption classifications, the one with a high AS has a greater probability of achieving its development objectives than the one with a low AS.

5.16 The portfolio of projects in execution for each year was therefore organized into six categories of probability in terms of achieving their development objectives, in order to see how their relative frequency has evolved over the period under study. These categories, arranged by growing level of probability, are shown in Box 3.

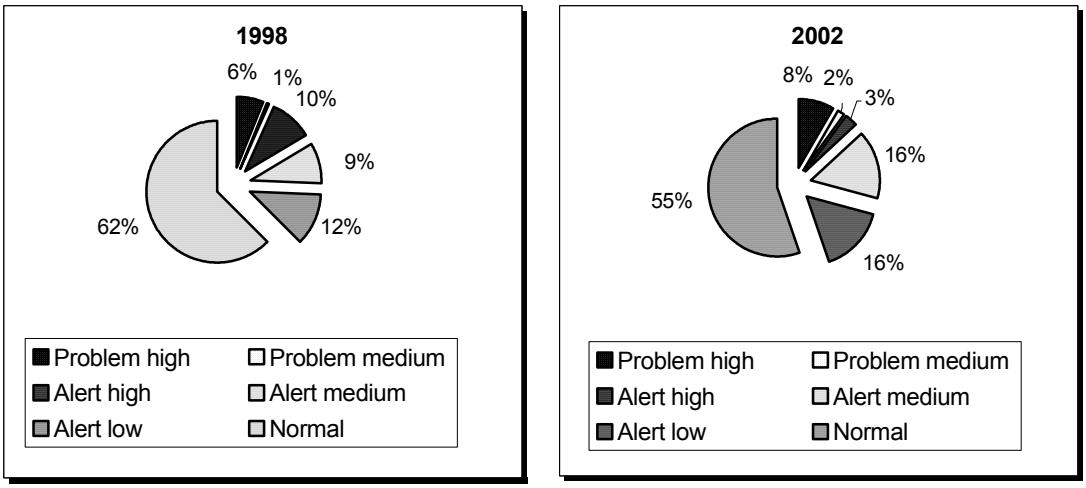
Box 3

Category	Classifications	
Problem high:	DOM, IPM	ASM
Problem medium:	DOM, any IP	ASB
Alert high:	DOB, IPM	ASM
Alert medium:	DOB, any IP	ASB
Alert low:	DOB, IPB	ASB, >= 2 PAIS param
Normal:	DOB, IPB	ASB

5.17 For purposes of visualizing the distribution trend, the following graph compares values for the two outer years of the period, 1998 and 2002.

5.18 The results show a decline of 7% in the relative weight of normal projects in the entire portfolio, explained essentially by the growing importance of projects with medium and low probability of alert and, to a lesser extent, by the increase in problem projects with a high probability of not achieving their development objectives (2%). In other words, the period produced an increase in development risk, with an internal distribution towards the categories of relatively lower risk.

Graph 10. Frequency Distribution of Development Risks



B. Evaluation of the development risk supervision system

5.19 The Bank's policies clearly indicate that the PPMR is the tool for supervision and monitoring project outcome risk mitigation efforts.

5.20 While there is no precise definition, three levels of risk are considered, reflecting the probability or certainty of achieving development objectives.

5.21 The portfolio at risk consists of projects on execution-risk status and alert status, plus problem projects that are likely to be restructured, reformulated, or canceled, in whole or in part. The latter fluctuated over the period at around 10% of the value of the approved portfolio in execution. It was found that problem projects have a high probability of escaping that status as they move nearer to completion. This is because such projects are considered as being "at risk", and not as projects where it is certain that their benefits will not recoup their costs.

5.22 It was also found that projects that end up in problem status were not necessarily classified as such at the outset. Most of the projects that ended up in problem status were initially classified as normal. This justifies the efforts that the Bank is making to refine the project at-risk concept, incorporating an analysis of projects classified as normal by Management, as ROS has been doing.

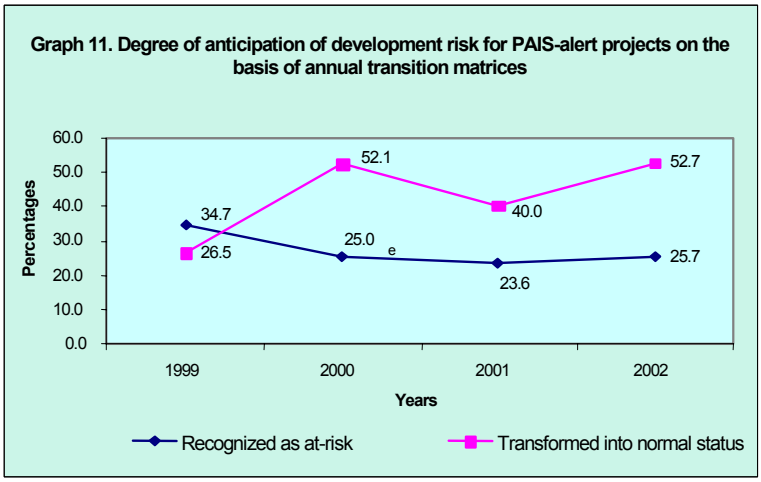
5.23 In recent years, the Bank has been reinforcing ROS's efforts to monitor portfolio execution management, in order to target it more directly at achieving outcomes and involving borrowers more closely in the entire process. Thus, ROS introduced a broader treatment of project risk, adding to the PAIS alert status the concept of risk in normal projects, for those that fail to meet two or more of eight parameters relating to disbursement delays.

5.24 This has led to the use of two systems for identifying execution risks: although they are supposed to be complementary, their convergence is not clear in reality. Measurements using those two systems produce different interpretations of development risks. Those risks have been significant and growing, and in 2002 they involved 194 projects (150 in execution-risk or PAIS status, and 44 in problem status), declining to 126 projects if only the PPMR classification is used (82 in execution-risk status and 44 in problem status). This would place the value of the approved portfolio in execution with some level of execution risk at US$17.85 billion (including US$4.569 billion in problem projects), a figure that declines to US$11.441 billion if only projects recognized as at-risk in the PPMRs are considered.

5.25 The PAIS early warning system has significantly increased (nearly doubled) the portfolio of projects recognized by the Operations Department as being in some situation of risk.

5.26 The annual portfolio at risk represents a significant percentage of the total approved portfolio in execution in 2002 in the sample projects ($37.028 billion). The situation confirms the importance of mitigating the risks in the approved portfolio in execution.

5.27 Given the resulting gap between the two measures of the portfolio at risk, a more detailed analysis was undertaken of the set of normal projects on alert in the PAIS system, which anticipates at-risk projects that are not flagged at that time in the PPMRs. Annual transition matrices were used for this purpose, covering the period 1998-2002, showing the changes produced in the normal projects on PAIS alert in any year, compared to their classifications in the following year.



5.28 The results show that around 25% of normal projects on PAIS status in one year are recognized in the following year by the PPMRs as being at risk (execution risk and problem status). Of this 25%, approximately 40% relates to projects in problem status or with low probability assumptions in the following year. At the same time, about 50% of projects declared on PAIS alert in one year (especially since 2000) will become normal projects the following year.

5.29 These results show that measuring projects on PAIS alert reveals a significant proportion of projects at development risk that the Bank's Management had not identified. This in itself justifies the centralized monitoring that the Bank conducts through ROS, using criteria that in some cases have been shown to be associated with project development risk.

5.30 On this basis, the analysis was pursued further, using the processed information. The findings lead to some considerations about how each of the eight parameters of the PAIS system contributes to defining the portfolio at execution risk.

Table 13

Frequency distribution of the PAIS alert parameters
as per status in last report on projects on alert (without repetitions)

Frequency	PAIS Parameters								Total
	1	2	3	4	5	6	7	8	
(Nº)	25	55	48	125	12	35	106	26	432
(%)	5.8	12.7	11.1	28.9	2.8	8.1	24.5	6.0	100.0

As per total status changes recorded for projects on alert (with repetitions)

Frequency	PAIS Parameters								Total
	1	2	3	4	5	6	7	8	
(Nº)	221	277	300	622	81	107	591	158	2,357
(%)	9.4	11.8	12.7	26.4	3.4	4.5	25.1	6.7	100.0

5.31 The variability of the frequency distribution (with and without repetitions) of the eight parameters in the universe of normal projects declared on alert suggests some further comments. First, the eight PAIS parameters do not exhibit the same frequencies, i.e. they do not have the same probability of occurrence and therefore do not carry the same weight. There is clearly a higher frequency of occurrence for parameters 4 and 7, and to a lesser extent for parameters 2 and 3. These findings point to the arbitrariness of the rule whereby a project is placed on alert status if it meets any two or more of the eight parameters.

5.32 Second, the results presented in Annex B to this report seem to confirm the inadequacy of parameters 5 and 6. These are regarded as alert indicators on the basis of execution values that diverge sharply from actual normal values. Third, parameter 8 is not the most relevant indicator for reflecting the importance of resource use in identifying development risk. AUG recommends introducing indicators that reflect the use of financial supervision in the opinions issued through the PPMR, thereby reducing the lack of contact between the two broad areas of risk that are monitored.

5.33 A final comment arises from considering which parameters were predominantly associated with normal projects that, having been placed on PAIS alert, were subsequently recognized as such by Operations Management. The results confirm that parameters 5, 6, and 8 are relatively unimportant, and that parameters 3, 4, and 7 (and to a lesser extent 1) are significantly associated with development risk.

5.34 In conclusion, the two systems defining the portfolio at execution risk, the one used by ROS and the one arising from the PPMRs, approach the same problem from different viewpoints. The percentage of projects on PAIS alert recognized by Operations Management (25%) alone confirms the importance of monitoring the project classification supervision by ROS. Yet the differences in the assessment also point to the existence of: (i) methodological problems and asymmetry of information in the PAIS parameters, which are recorded automatically from the circumstances that are reported differently in the PPMRs; and (ii) sufficient empirical evidence to justify a review of the content and reliability of the views expressed in the PPMRs.

VI. MANAGEMENT OF RISK-BASED SUPERVISION

6.1 This chapter assesses three important aspects in order to form an opinion as to whether the Bank is conducting its supervision in such a way as to anticipate and mitigate development risks.

6.2 First, it examines the degree to which supervision instruments are used in projects at risk of not achieving their development objectives each year (static analysis). Next, it introduces a dynamic analysis to see how the Bank's planned or mandatory

supervision activities respond once the project is identified as at risk. Lastly, it measures the impact of the supervision performed, to determine the extent to which it has helped to improve the risk classification of projects so identified.

A. The use of supervision in projects at risk

6.3 The methodology adopted consisted in comparing the annual use of three of the Bank's typical supervision instruments (administration missions, technical inspection visits, and annual portfolio review missions), with the project classification based on the development risk rating (execution risk or alert, problem and normal status).

6.4 The results show that the three supervision products for projects classified in the at-risk portfolio were used to differing degrees: the tool most frequently associated with risk mitigation is the CPR, which was performed for about 70% of projects classified at risk. Technical inspection visits were conducted for only 55% of projects at risk, while the figure for administration missions from headquarters is only 17%.

Table 14
Use of Oversight as a Function of Risk, 1998-2001
(Static analysis)

Monitoring tool/project classification	1998		1999		2000		2001		1998-2001
	No. of projects	No. of projects with monitoring	No. of projects	No. of projects with monitoring	No. of projects	No. of projects with monitoring	No. of projects	No. of projects with monitoring	Average degree of monitoring (%)
Administration Missions									
Execution risk	112	13	119	23	128	24	137	25	17.1
Problem	28	6	38	12	51	12	40	9	24.8
Normal	258	45	248	52	277	42	311	38	16.2
Total	398	64	405	87	456	78	488	72	17.2
Technical Inspection Visits									
Execution risk	112	48	119	59	128	79	137	89	55.4
Problem	28	13	38	19	51	18	40	23	46.5
Normal	258	109	248	110	277	126	311	149	45.2
Total	398	170	405	188	456	223	488	261	48.2
Annual Portfolio Review Missions									
Execution risk	112	80	119	68	128	96	137	106	70.6
Problem	28	17	38	17	51	44	40	31	69.4
Normal	258	198	248	170	277	229	311	252	77.6
Total	398	295	405	255	456	369	488	389	74.9

6.5 There are no great differences of frequency between the two risk components (alert and problem). Further conclusions are that: little use is made of supervision missions for problem projects; the extent to which the Bank's policy-mandated supervision instruments, and especially the technical inspection visits, are used falls well short of 100%; and there is little planning of special administration missions for projects at risk.

B. The supervision response to identified risks

6.6 The static analysis was supplemented by a dynamic analysis over time to address two questions: first, whether Management responds to the risks identified in one

year by stepping up supervision activities in the next year; and second, whether the results of those supervision activities lead to improvements in the classification of projects at risk (an aspect that is developed in the following point).

6.7 The methodology used for measuring the supervision response to risk involved analyzing two consecutive years to see what happened with supervision activities in the year following the one in which the project was placed on alert or problem status. The analysis considered only administration missions and technical inspection visits. The results, when compared with those from the previous static analysis, can be used to determine whether the Bank conducts supervision in such a way as to anticipate risks, or merely to mitigate those that have been identified.

6.8 The measurement indicator used, the "Degree of Supervision Response to Risk", was calculated as the ratio between the number of projects supervised in one year and the number of projects still in execution during that year that had been on alert or problem status the year before.

6.9 The results show significant improvements in the response rate, compared to that from the static analysis. With respect to technical inspection visits, depending on the year, these were conducted for some 70% of the portfolio at risk, reaching a rate of 81% in 2001. For problem projects the growth rate was lower, but perceptibly greater than in the static analysis.

6.10 The same response emerges from considering administration missions, although to a lesser extent than with inspection visits. Moreover, it was better in the case of problem projects than in those on execution alert, suggesting that headquarters takes a more active role in projects with a high probability of being reformulated or canceled.

Table 15
The Oversight Response to Identified Risks, 1998-2001
(Dynamic analysis)

Monitoring tool/project classification	1998-1999				1999-2000				2000-2001			
	Nº of projects at risk			Degree of oversight response to risk (%)	Nº of projects at risk			Degree of oversight response to risk (%)	Nº of projects at risk			Degree of oversight response to risk (%)
	In 1998 [1]	In execution in 1999 [2]	With monitoring in 1999 [3]	[4]=[3] / [2]	In 1999 [1]	In execution in 2000 [2]	With monitoring in 2000 [3]	[4]=[3] / [2]	In 2000 [1]	In execution in 2001 [2]	With monitoring in 2001 [3]	[4]=[3] / [2]
Administation missions												
Execution risk	112	94	23	24.5	119	103	27	26.2	128	109	18	16.5
Problem	28	21	11	52.4	38	34	9	26.5	51	38	15	39.5
Total	140	115	34	29.6	157	137	36	26.3	179	147	33	22.4
Technical inspection visits												
Execution risk	112	94	66	70.2	119	103	72	69.9	128	109	88	80.7
Problem	28	21	17	81.0	38	34	16	47.1	51	38	26	68.4
Total	140	115	83	72.2	157	137	88	64.2	179	147	114	77.6

6.11 The results show improvement in the response of both supervision instruments when projects are identified as at-risk. This confirms that supervision is directed more towards risk mitigation than risk anticipation, a result that contrasts sharply

with the low level of compliance in the use of these compulsory products, as noted earlier.

C. The impact of supervision on project risk classification

6.12 Indicators were aggregated to provide more information on the effectiveness of Management's periodic supervision activities in terms of improving projects on execution alert.

6.13 The methodology involved constructing annual transition matrices of classification changes for projects at risk. These classifications were arranged in accordance with the use of the two periodic supervision instruments selected as representative of the Bank's monitoring activities (administration missions and technical inspection visits).

6.14 For each supervision tool, three transition matrices were constructed from available information covering the periods 1998-1999, 1999-2000, and 2000-2001. The main body of the matrix in the table shows the classification change by number of projects. The right-hand panel shows the degree of association of each tool with improvements in project risk classification.

6.15 For administration missions, they would not seem to be closely associated with improvements in the classification of projects declared at execution risk at the end of the preceding year since the rate of correspondence is only one-third.

Table 16
Number of administration missions and changes in project risk classification
Annual transition matrices for classification risk, 1998 to 2001

			1999									Contribution of MA to improvements in classification (%)		
			Projects at execution risk			Problem projects			Normal projects					
	Classification	Nº of projects	w MA	w/o MA	Total	w MA	w/o MA	Total	w MA	w/o MA	Total	w MA	w/o MA	Total
1998	Execution risk	94	14	51	65	2	3	5	7	17	24	7.4	18.1	25.5
	Problem	21	2	3	5	6	7	13	3	0	3	23.8	14.3	38.1
	Total	115	16	54	70	8	10	18	10	17	27	10.4	17.4	27.8

			2000									Contribution of MA to improvements in classification (%)		
			Projects at execution risk			Problem projects			Normal projects					
	Classification	Nº of projects	w MA	w/o MA	Total	w MA	w/o MA	Total	w MA	w/o MA	Total	w MA	w/o MA	Total
1999	Execution risk	103	13	46	59	5	7	12	9	23	32	8.7	22.3	31.1
	Problem	34	3	10	13	4	10	14	2	5	7	14.7	44.1	58.8
	Total	137	16	56	72	9	17	26	11	28	39	10.2	27.7	38.0

			2001									Contribution of MA to improvements in classification (%)		
			Projects at execution risk			Problem projects			Normal projects					
	Classification	Nº of projects	w MA	w/o MA	Total	w MA	w/o MA	Total	w MA	w/o MA	Total	w MA	w/o MA	Total
2000	Execution risk	109	11	51	62	3	8	11	4	32	36	3.7	29.4	33.0
	Problem	38	6	5	11	5	13	18	4	5	9	26.3	26.3	52.6
	Total	147	17	56	73	8	21	29	8	37	45	9.5	28.6	38.1

Note: Covers MAs performed each year, planned or not

6.16 This does not hold for the association of MAs with problem projects: here, the correspondence with improved classification exceeds 50% for projects in the last two periods, and is 38% for the first period. Thus, MA is more closely associated

with classification improvements for problem projects. The results also indicate that project reformulation or cancellation is the least-expected outcome.[33]

6.17 With respect to Technical Inspection Visits, the analysis is rather more complex, since Bank policies establish a minimum of one visit per year, without setting a ceiling on their number. This aspect was introduced into the transitional matrices by distinguishing between projects for which the number of visits exceeded, equaled, or fell below the number in the previous year.

6.18 The results show that, in contrast to administration missions, technical inspection visits correlate with two-thirds of classification improvements from the previous year, both for projects on alert and for problem projects. The proportion of projects that improve their alert classification over the three 2-year periods varies between 21% and 29% of all projects with that classification in the preceding year. This figure is significantly higher for problem projects, where classification improvement varies between 38% and 53%, depending on the period in question.

Table 17
Number of technical inspection visits and changes in project risk classification
Annual transition matrices for classification risk, 1998 to 2001

			1999												Contribution of IVT to improvements in classification (%)			
			Projects at Execution Risk				Problem Projects				Normal Projects							
			with IVT		w/o IVT	Total	with IVT		w/o IVT	Total	with IVT		w/o IVT	Total	with IVT		w/o IVT	Total
	Classification	Nº of projects	>	=<			>	=<			>	=<			>	=<		
1998	Execution risk	105	30	18	29	77	1	1	3	5	9	7	7	23	8.6	6.7	6.7	21.9
	Problem	24	2	1	2	5	7	5	3	15	2	0	2	4	16.7	4.2	16.7	37.5
	Total	129	**32**	**19**	**31**	**82**	**8**	**6**	**6**	**20**	**11**	**7**	**9**	**27**	**10.1**	**6.2**	**8.5**	**24.8**

			2000												Contribution of IVT to improvements in classification (%)			
			Projects at Execution Risk				Problem Projects				Normal Projects							
			with IVT		w/o IVT	Total	with IVT		w/o IVT	Total	with IVT		w/o IVT	Total	with IVT		w/o IVT	Total
	Classification	Nº of projects	>	=<			>	=<			>	=<			>	=<		
1999	Execution risk	107	29	21	16	66	6	2	6	14	7	7	13	27	6.5	6.5	12.1	25.2
	Problem	38	6	4	3	13	3	0	15	18	2	1	4	7	21.1	13.2	18.4	52.6
	Total	145	**35**	**25**	**19**	**79**	**9**	**2**	**21**	**32**	**9**	**8**	**17**	**34**	**10.3**	**8.3**	**13.8**	**32.4**

			2001												Contribution of IVT to improvements in classification (%)			
			Projects at Execution Risk				Problem Projects				Normal Projects							
			with IVT		w/o IVT	Total	with IVT		w/o IVT	Total	with IVT		w/o IVT	Total	with IVT		w/o IVT	Total
	Classification	Nº of projects	>	=<			>	=<			>	=<			>	=<		
2000	Execution risk	111	32	20	16	68	2	6	3	11	16	12	4	32	14.4	10.8	3.6	28.8
	Problem	44	3	5	4	12	8	6	11	25	2	2	3	7	11.4	15.9	15.9	43.2
	Total	155	**35**	**25**	**20**	**80**	**10**	**12**	**14**	**36**	**18**	**14**	**7**	**39**	**13.5**	**12.3**	**7.1**	**32.9**

Note: Calculated on the basis of the number of IVTs performed for each uncompleted project in each year, with respect to the previous year.

6.19 Conducting, or increasing the number of, IVTs is correlated more closely with classification improvements for projects at development risk. Given this positive association, it would seem important to make use of this type of supervision tool, a conclusion that belies the low degree of compliance observed in its use, despite the fact it is compulsory.

D. Supervision of execution and risk management

6.20 The risk to the annual portfolio in execution is great and growing, and a significant portion of that risk is subject to differing interpretations by the Bank's departments.

[33] Of all projects in execution in 1998-2001 covered by the sample for this evaluation (616 projects), only 20 projects were reformulated in terms of their development objectives.

6.21 The response in terms of the use of supervision instruments for projects at risk is low, focusing essentially on the CPRs, which are essentially risk mitigation milestones. This fact defines two key features of development risk management: first, that the Bank does not use typical risk-forecasting instruments; and second, that because it does not anticipate risks it acts essentially to mitigate them, thereby depriving development risk management of its timeliness and continuity.

6.22 This point is confirmed in the information presented, which shows that supervision becomes more dynamic once the project is declared to be at execution risk or with problems.

6.23 As a mechanism for mitigating risk, it was found that the Bank's supervision is associated more with changes in classification of problem projects than with projects placed on execution alert. For Management, the scenario least expected is one involving the reformulation of development objectives or project cancellation.[34]

6.24 The high correlation between the number of at-risk projects that improve their classification and the performance or increase of technical inspection visits (especially for projects placed on alert in the previous period) highlights the fact that widespread use of this tool is important for risk management.

VII. CONCLUSIONS AND RECOMMENDATIONS

A. Summary of evaluation results

1. Lack of an explicit supervision system

7.1 That there is no single, comprehensive document describing the supervision system, or overview of the process outlining the relationships between activities underpinning the products of supervision makes it difficult to report on actions and their results to project managers. This leads to differing interpretations of the basic principles, how they function, and their scope, update methods, the relationship between the instruments, or accountability for information and results.

2. The information system for supervision instruments is inefficient

7.2 The supervision information system is incomplete. It is spread around in different places and file forms, and is therefore not readily accessible. It is not a reliable management tool because:

- The databases identified do not contain information on all instruments, and much of the information that does exist is out of date.

[34] This can also be demonstrated in the significant proportion (64%) of declared problem projects that improve the probability of achieving their development objectives (see Chapter V).

- The information system does not function as a single center with interconnected local networks to allow for automatic updating, easy access, and the production of key supervision indicators to facilitate monitoring and evaluation.

- There is a wide range of proprietary designs with information stored in inconsistent files, of questionable validity.

- The operations managers use a tool-based rationale, not one based on an information system; information is organized in inventories by supervision tool or set of instruments that are not closely related.

- Isolated operations do not lend themselves to the economies of scale evident in tasks of this kind, with the result that it is not cost efficient and user demands cannot always be met.

3. The information system is of little help in verifying compliance of supervision activities

7.3 The supervision information system will not permit verification to ensure that supervision activities are performed as required under the Bank's policies and regulations.[35] Accordingly, the system is of little use in reporting and information flow does not need to be timely for use in anticipating and managing operational risks because:

- The information system does not function on the basis of time-sensitive procedures indicating when a particular activity needs to be performed in accordance with policy or because they were anticipated in the project planning process.

- There are no systems to monitor the performance of supervision activities at the level of the Regional Operations Departments.

- There is no system manager who consolidates, reports, and monitors all execution risks.

- There is a single central unit (ROS) responsible for part of the information system, which has been moving into areas, improving developments, and reporting to Senior Management on the different supervision instruments used by the Regional Operations Departments.

[35] A significant investment of time and resources by OVE was required to construct an information system that would allow this evaluation objective to be fulfilled, while at the same time preventing it from falling victim to the "information dilemma."

4. The level of compliance of supervision activities is low

7.4 Not more than 75% of the supervision activities identified in Bank policies and regulations are performed. The main reasons for this are listed below:

- The use of supervision instruments is uneven, and only two attain values approaching 100% of activities completed (PPMR and PCR).

- Project supervision activities are not scheduled frequently and even less so if measured by scheduled activities actually completed. While the Bank completes 81% of minimum supervision activities considered mandatory under Bank policies, it completes only 43% of those scheduled as part of a project.

- The relationship between the increased number of supervision activities and the rate of noncompliance observed in supervision activities can be ascribed to a number of factors that need to be compared with one another (i.e. uneven growth in installed capacity, ad hoc planning based on risk or a different interpretation of the relative importance of the instruments).

- The findings suggest that the quantity, design, and operational appropriateness of mandatory instruments are neither consistent with one another nor compatible with the rationale of the supervision function.

- Low completion rates and insufficient information undermine the capacity of the Regional Operations Departments to fulfill their fiduciary responsibilities.

5. Supervision instruments are not used consistently

7.5 The way in which the instruments of supervision are used bears little relation to the process involved since it is not commensurate with the logical steps in the supervision process. The main reasons are:

- PPMRs are not prepared primarily on the basis of preinspection visits. There were on average IVTs for 67% of projects with PPMRs, and IVFs for 29% of that total.

- Initial planning and execution missions are infrequent. The MS were carried out for 25% of projects initiated in 1998-2001, an indication of Management's concern in recent years about increasing the number of such activities.

- Only 78% of annual country portfolio reviews (CPRs) were carried out in the borrowing member countries. Failure to carry out CPRs means that opportunities are missed for dialogue between the Bank's Senior

Management and the country on execution risks and that inputs used to prepare the PPMRs are not used.

- The content of the CPRs overlaps with that of the APEs, and the aims and objectives of the former are not fulfilled in their entirety, whereas those of the latter are; yet the CPRs are not discussed with the country authorities. This discrepancy detracts from the importance of CPRs, which are key documents for reporting on the results of dialogue with the countries.

- Financial inspection visits to projects with qualified EFAs was just 50% of the total.

6. Low rate of use of supervision tool for evaluation of outcomes and of borrower-linked supervision

7.6 The Bank supervises the attainment of development targets with instruments linked to self-evaluation (primarily PPMRs and PCRs), in which there is no beneficiary participation or participation is voluntary.[36] Planning the use of instruments for supervision of the results of operations is very low, and the figure is one third lower taking into account activities that are fully executed.

7.7 The use of borrower-linked supervision instruments rose steadily during the period, but the levels attained are still low. More than 50% of possible activities are not executed, with dialogue focusing on CPRs, which have become the main mechanism used by Bank authorities to address project problems and risks.[37]

7. Risk information is scattered and lacks ownership

7.8 Information on the annual execution of operations shows the Bank to be an institution that assumes risk, which is not a problem per se. What is problematic, however, is that the information on risk flowing to risk management centers is not timely and is incomplete, deriving from various sources that do not interface with one another. This is because:

- 48% of annual disbursements for loans in the study sample experienced problems of some kind with funds administration, either because they lacked EFAs (19%) or else, having them, they were qualified (29%).[38] As a trend, these figures rose throughout the period. In the management reports produced

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[36] The Bank has recently been promoting, as a common practice, greater contact and consultation with the beneficiaries in preparing the aforementioned instruments, which has resulted in improvement.

[37] This does not mean overlooking the ongoing dialogue the Country Offices have in the countries. This conclusion refers to the small degree to which borrowers participate in the supervision products.

[38] The 48% figure drops to 37% of annual disbursements if the EFA ratings are adjusted for the opinions issued by the COs upon rating such opinions in accordance with the binary rating system defined by ROS.

by ROS, only the EFA completion rate is reported, and as such, it is used as a parameter to red flag potential project problems.

- Every year, 48% of the amount approved for projects in execution (45% based on the number of projects) experience some type of development risk, either because the project has been declared subject to execution risk, or on state of alert (36%), or because it has been classified as a problem project (12%).[39] These figures increased during the period. The information is not reported in this way,[40] and there is usually a tendency to interpret the active portfolio risk as the project rating upon completion.

- On average, project execution has been requiring some 50% more time than originally scheduled, which may expose implementation to uncertainties not anticipated in the operational design and lower the return on the project's net benefits.

- Information on project execution risks comes from various sources, many of them unrelated to each other.[41] What is striking is the absence of a risk-based management control despite the magnitude of the risk that has been identified.

8. There are various interpretations of one single type of risk

7.9 A significant proportion of the risks are not evaluated in the same way by all of the Bank's departments.

- The supervision of fiduciary aspects has different interpretations of the rating of independent opinions on project financial statements (EFAs). Moreover, financial inspection visits were not the primary supervision tool used for monitoring.

- The procedures for identifying projects at risk (PPMR and PAIS alert) show inconsistent results during the period under review.

- Fiduciary risk is not related to project development risk in supervision instruments. Fiduciary risk is defined solely according to its validity and relevance to the eligibility of the expense and its proper posting in the

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[39] If we consider only projects at risk based on the PPMRs (i.e., excluding normal projects on PAIS status) that percentage falls to 31% of the value of the approved portfolio for projects in execution.

[40] Document GN-2215-1 shows the concern for having indicators that begin to clearly measure the above.

[41] From 1998 to 2001, an average of slightly over 10% of projects in execution per year faced simultaneous financial and development risk. If we include projects subject to financial or development risks, we find that 52% of projects faced one or the other of the two risks. This information came from four different sources, which are normally not related to each other.

financial statements. The allocation of funds to execution, however, bears no relation to the objectives or the components of the project for which they were granted.

9. Supervision management does not adequately anticipate risks

7.10 Risk management was found to be most effective when projects are declared subject to execution risk. The report shows that supervision activities that anticipate risk are used infrequently, and that, when risks materialize, the information is not shared sufficiently with others or within the Bank itself. This situation makes supervision a mitigative tool, rather than a preventive one. This finding is based on the following information:

- The anticipation of risks is associated more closely with symptoms (for example, disbursement problems, etc.) than with their relationship to development risks.

- Insufficient planning and few initial missions, a factor that affects execution.

In management reports, only some of the financial risks are shared with others, those related to EFAs that have not been completed.

- The absence of a link between IVFs and projects at financial risk demonstrates a lack of interface between the planning and execution of the former with the latter.

- IVTs and IVFs prepared by the COs are not shared sufficiently with the borrowers and Regional Operations Departments.

- Dynamic analysis used for evaluation[42] confirms that the completion, planning, and execution of supervision instruments, in the face of changes in project risk, are most effective once the project is declared as being at risk.

10. The evaluation was unable to find an independent system of internal control for supervision activities or standards of internal control that certify the effectiveness of supervision

7.11 In the institutional context, there is no system of internal control independent of the process of supervision of Bank activities. Internal control of supervision focuses on the same staff that are responsible for operations management.

7.12 No formal frameworks or standards are used to certify periodically the effectiveness of the controls of execution activities and supervision, verifying whether resources

[42] See Chapter VI.

were effectively used for development purposes in accordance with strategic objectives and institutional policies.

B. Conclusions

7.13 The principal conclusions are:

- The Bank does not have an integrated and independent supervision system to anticipate risk. This renders management of much of the portfolio and the Bank's decision-making process ineffective.

- As there is no formal system of consolidated supervision, it is not clear who is responsible for risk supervision and management and how the different instruments relate to one another.

- Because project management is not based on risk assessment, the supervision instruments that exist are inconsistent with the supervision function and therefore inefficient and less cost effective.[43]

- There is no integrated, transparent, and readily accessible information system that can be used to anticipate and manage risk as well as to verify the extent to which supervision and internal control functions have been fulfilled.

- The Board of Executive Directors and Senior Management are not kept regularly informed on these specific issues.

- That shortcomings have been identified in the present system does not mean that the Bank does not supervise its operations but that, institutionally, supervision is ineffective.

- As supervision is based mainly on mitigating contingencies as they arise, the procedures set out in Bank manuals and standards are not fulfilled and mechanisms not formally approved but considered more suitable by Management to correct such contingencies come into play. Paradoxically, such

[43] The mandatory supervision instruments are compulsory for all operations, and are accorded equal importance with a similar level of risk in all operations, which minimizes the impact of the risks on portfolio management.

mechanisms are virtuously associated with the risk-based supervision function.[44]

C. International practices

7.14 A survey of international experiences found that the situation within the Bank is not in line with the best practices of other multilateral development banks, international development agencies, and donor countries. In particular:

WHAT IS THE COMMITTEE OF SPONSORING ORGANIZATIONS OF THE TREADWAY COMMISSION (COSO)

COSO is a voluntary private sector organization established in USA. It is dedicated to improve the quality of the process of internal control designed to provide reasonable assurance regarding the following corporate objectives: (i) reliability and integrity of financial reporting; (ii) compliance with policies, plans, procedures, laws and regulations; (iii) effectiveness and efficiency of operations; and, (iv) the safe guarding of assets.

The internal control components of COSO are:

Control Environment establishes the foundation, the structure and incentives, for the internal control system, based on clearly articulated institutional objectives.
Risk assessment involves the identification and analysis of relevant risks to achievement objectives and forms the basis of how risks should be managed.
Control Activities are the policies, procedures and practices that ensure that management's directives are carried out and the institution's mandate is fulfilled.
Monitoring involves external oversight of the internal controls or use of independent methodologies within the process to measure whether controls are adequate and the objectives are being met.
Information & Communication support the other four objectives by communicating the necessary information in a timely, digestible way that enables staff to perform their functions.

- Various multilateral institutions and organizations have addressed these issues by creating an internal control environment that requires compliance with corporate objectives. Noteworthy in this respect are the components of internal control established by COSO (Committee of Sponsoring Organizations of the Treadway Commission), a private sector organization established in the United States to measure the quality of internal control and thereby enhance the reliability and integrity of financial reports, verify compliance with the organization's policies, procedures, and regulations, confirm the effectiveness and efficiency of operations, and safeguard the organization's assets.

- Another factor that highlights the shortcomings in Bank supervision and its internal control system is depicted in the Bank for International Settlements update on sound practices in which recommendations are made on the management and supervision of operational risk (February 2003).

- The World Bank has been developing an implementation organization based on risk assessment. It operates at three interacting levels: project programming and

[44] In fact, empirical analysis suggests that the project supervision carried out is related to the ad hoc organization of supervision in response to risks effectively produced, given their essentially mitigatory nature. This situation is also associated with a broadening the boundaries and the informal nature of the supervision system, based on the use of informal or other supervision procedures considered to be more effective than the mandatory ones. Such procedures are not thrown together systematically in the institution's formal supervision instruments or stored in standard information technology databases. This makes the system less formal and creates an environment that does not lend itself to fulfillment of supervision commitments.

implementation, the country (and region), and the corporate level. At the first level, the evaluation considers three types of risks: development effectiveness risks, fiduciary risks, and safeguard risks, developing specific procedures and products for each type. At the second level (the country) there are a series of instruments for evaluating political, social, technical, financial, and natural risks involved in project implementation. Of particular interest are the analysis of country risk, the financial accountability assessment, the country procurement assessment; and the public expenditure review. The system also involves a country performance assessment for guidance in the allocation of concessional resources, and economic and sector studies together with the country assistance strategy (CAS). At the third or corporate level, there are various instruments, including: a quality assurance group to improve control activities; a senior-level committee to manage strategic risks relating to institutional policies and objectives, as well as risks that affect the institution's reputation; the supervision of the Board, through the Audit Committee and the Committee on Development Effectiveness; the Operations Evaluation Department which attests to the adequacy of risk management arrangements and whose annual report (AROE), since 2001, has been configured to provide input, at the corporate level, to the COSO cycle; reporting since 1996 on the effectiveness of internal controls, using the COSO methodology; the Country Assistance Evaluation (CAE), which is sequenced to provide input for the CAS; and the production of reports on sector evaluations.

Sound Practices for the Management and Supervision of Operational Risk.
Bank of International Settlements, February 2003

Developing an Appropriate Risk Management Environment[1]

Principle 1: The board of directors 1/ should be aware of the major aspects of the bank's operational risks as a distinct risk category that should be managed, and it should approve and periodically review the bank's operational risk management framework. The framework should provide a firm-wide definition of operational risk and lay down the principles of how operational risk is to be identified, assessed, monitored, and controlled / mitigated.

Principle 2: The board of directors should ensure that the bank's operational risk management framework is subject to effective and comprehensive internal audit by operationally independent, appropriately trained and competent staff. The internal audit function should not be directly responsible for operational risk management.

Principle 3: Senior management should have responsibility for implementing the operational risk management framework approved by the board of directors. The framework should be consistently implemented throughout the whole banking organization, and all levels of staff should understand their responsibilities with respect to operational risk management. Senior management should also have responsibility for developing policies, processes and procedures for managing operational risk in all of the bank's material products, activities, processes and systems.

Risk Management: Identification, Assessment, Monitoring, and Mitigation/Control

Principle 4: Banks should identify and assess the operational risk inherent in all material products, activities, processes and systems. Banks should also ensure that before new products, activities, processes and systems are introduced or undertaken, the operational risk inherent in them is subject to adequate assessment procedures.

Principle 5: Banks should implement a process to regularly monitor operational risk profiles and material exposures to losses. There should be regular reporting of pertinent information to senior management and the board of directors that supports the proactive management of operational risk.

Principle 6: Banks should have policies, processes and procedures to control and/or mitigate material operational risks. Banks should periodically review their risk limitation and control strategies and should adjust their operational risk profile accordingly using appropriate strategies, in light of their overall risk appetite and profile.

Principle 7: Banks should have in place contingency and business continuity plans to ensure their ability to operate on an ongoing basis and limit losses in the event of severe business disruption.

Role of Supervisors

Principle 8: Banking supervisors should require that all banks, regardless of size, have an effective framework in place to identify, assess, monitor and control/mitigate material operational risks as part of an overall approach to risk management.

Principle 9: Supervisors should conduct, directly or indirectly, regular independent evaluation of a bank's policies, procedures and practices related to operational risks. Supervisors should ensure that there are appropriate mechanisms in place, which allow them to remain apprised of developments at banks.

Role of Disclosure

Principle 10: Banks should make sufficient public disclosure to allow market participants to assess their approach to operational risk management.

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[1] This paper refers to a management structure composed of a board of directors and senior management. The Committee is aware that there are significant differences in legislative and regulatory frameworks across countries as regards the functions of the board of directors and senior management. In some countries, the board has the main, if not exclusive, function of supervising the executive body (senior management, general management) so as to ensure that the latter fulfils its tasks. For this reason, in some cases, it is known as a supervisory board. This means that the board has no executive functions. In other countries, the board has a broader competence in that it lays down the general framework for the management of the bank. Owing to these differences, the terms 'board of directors' and 'senior management' are used in this paper not to identify legal constructs but rather to label two decision-making functions within a bank.

RISK ASSESSMENT IN THE WORLD BANK

Risk Assessment at:	Instruments
Projects in Pipeline and Implementation	**Related to Development Effectiveness Risks** # Quality Control Process 1/ #Assessment in adjustment operations 2/ # CPPRs and PAR 3/ # M&E: quantitative performance indicators **Related to Fiduciary Risks** # Financial Management Assessment (FY02) **Related to Safeguard Risks** # System of insuring compliance (FY01) 4/ # QACU (Quality Assurance and Compliance Unit)
Country Level 5/ 6/	# Credit Risk Analysis # CFAA (Country Financial Accountability Assessment) # CPAR (Country Procurement Assessmente Report) # PER (Public Expenditure Reviews) # Performance Assesment as a guide for allocating IDA resources # ESW products (Economic and Sector Work) # CAS (Country Assistance Strategy)
Corporate Level 5/	# QAG (Quality Assurance Group) to improve control activities of projects(monitoring) for internal quality Assurance/Enhancement of Lending. #Management Committee at the senior level to address risks related to development effectiveness and reputation 7/ # Oversight of the Board through the Audit Committee and CODE (Committee of Development Effectiveness) # OED (Operations Evaluation Department) to attest to the adequacy of risk management arrangements. # Reporting on internal controls since 1996, using the COSO (Committee of Sponsoring Organizations of the Treadway Commision) framework # AROE (Annual Report of Operations Evaluation) was configured to feed into the corporate COSO cycle.8/ # CAE (Country Assistance Evaluations) were sequenced to feed into the CAS (Country Assistance Strategy) cycle. # Sector Evaluations were geared to the production of Sector Strategic Papers.
Source: Based on "2002. Annual Report on Operations Evaluation-World Bank,OED; by Laurie Effron" and "The Logic of Renewal: Evaluation at the World Bank (1992-2002), by Roberto Picciotto".	
Notes: 1/ Peer Review; Several Layers of Management; Sensitivity Analysis 2/ Such as ownership of policy reform; capacity to comply with conditionality; linkage of policy reforms supported under Poverty Reduction Programme; acceptance of the reforms by the client's country 3/ Country Portfolio Peformance Review: country wide systemic risks to development effectiveness of ongoing projects and measures to adress them, suported by PAR (Portfolio at Risk) introduced in 1996 by QAG (Quality Assurance Group) 4/ Risk assessment include a safeguard risk review in each Region with assistance of QACU, QAG, QAE. Each Region has developing methods for assessing risks 5/ For all types of risks 6/ Political, social, technical, financial and natural risks relevant to each operation 7/ For the strategic risks of policies and corporate goals; identification of control gaps and overlapings that need attention 8/ With the objective or shorten the feedback loop of evaluation products to the business process of the institution	

- The World Bank's approach presents both similarities and differences with that of the IDB, but such an analysis is beyond the scope of this evaluation. By way of example, the following differences can be noted with respect to the IDB: operations are supervised on the basis of three types of risk, country risk control instruments are more diversified, and the environment for risk control at the corporate level is more clearly and fully described.

- The issue of internal control and of the need to use periodic mechanisms for independent external verification of its effectiveness has covered in recommendations to be incorporated into the monitoring of MDB lending operations. In particular, the GAO (United States General Accounting Office) has been making proposals of this kind, based on reports on the situation in the MDBs.

D. Recommendations

The conclusions of the present evaluation support the following recommendations:

- Develop an integrated system of execution supervision, based on a risk-based portfolio management approach that incorporates the best practices of other similar institutions.[45][46]

- Adopt an internal control framework model to improve governance within the Bank itself.

- Prepare a report, on a regular basis, to be presented to the Board of Executive Directors and Senior Management establishing the progress made in terms of i) the effectiveness of operations in contributing to the institution's strategic objectives and the extent to which its policies and standards have been observed; ii) management effectiveness based on risk evaluation and execution supervision; and iii) the cost efficiency of institutional management and supervision systems.

- Develop an integrated reporting system as a key component of the supervision system to support the recommendations noted earlier and to provide Bank staff with on-line information and guidance on the performance of management, supervision, and execution supervision functions.

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[45] These practices suggest that a systems of supervision needs to be established for execution of operations, independent of risk management, based on an assessment of risk. The system of supervision as part of the project cycle would be subject to independent internal control, using regulatory frameworks that will certify the quality of internal control procedures and of coordination with the organization's strategic policies and objectives. This internal control would in turn be subject to a systematic external control.

[46] Material references to this topic may be found in various documents published by the "Basel Committee on Banking Supervision" of the BIS; the Asian Development Bank's "Handbook for Integrating Risk Analysis in the Economic Analysis of Projects," in papers by the World Bank's OED, and several relating to risk assessment by the World Bank, as well as by other government agencies in Australia, the United Kingdom, and the United States. Private international consulting and auditing firms, such as Ernst & Young and Deloitte Touche Tohmatsu, have also made significant contributions to the topic.

IDENTIFYING THE BANK'S SUPERVISION SYSTEM

A. Introduction

The evaluation required, as a first step, identifying the products of the Project Execution Supervision System that make the evaluation objective. This calls for a detailed analysis of the supervision process in order to distinguish the products of supervision from the inputs used to produce them.

An initial difficulty was the absence of any single, comprehensive document setting out the rationale and the approach used in the Bank's execution supervision process. Components of that process are described in various manuals, policies and regulations of varying enforceability. These have been built up over time, with continuous updates to reflect problems encountered and lessons learned.

Reading the manuals and interviewing the people responsible for this function within the Bank revealed the existence of supervision products not mentioned in the relevant regulations, as well as differing understandings as to the limits of the supervision system. It was found that, although these people feel they form part of a whole, they interpret this in varying ways, and lack a collective understanding as to what the current version is.

The supervision model used by the Bank has purposefully focused on defining the actions it comprises, but it lacks a clear vision of the process, making it difficult to distinguish products from the inputs needed to prepare them. Existing manuals are better at explaining the "what" than the "why" of each supervision activity, or "how" those activities relate to each other.

These limitations have led to the use of a conceptual and methodological framework for organizing the products of supervision operations that provides project managers with information on the functioning and results of their projects.

B. Conceptual framework

The concept of project execution supervision underlying this report relates to the way in which the institution manages, on an ongoing basis, the risks involved in implementing operations approved by the Board of Executive Directors.

In a development institution such as the Bank, minimizing risk has to do with issues of three kinds: (i) risks concerned with the Bank's mission (development risks); (ii) risks that arise during project implementation (operational risks); and (iii) risks linked to the use of funds in accordance with the procedures and purposes for which they were intended (fiduciary risks).

All of these risk categories can exist separately, and each one has its own importance. For an institution like the Bank, however, the priority consideration is how those risks impact

on development objectives. According to this concept, risk is any problem that jeopardizes or reduces the possibility of achieving development objectives.

Supervision is a way of continuously linking project or program preparation with execution and evaluation at each stage of the project cycle, thereby verifying that execution is economical, efficient, and effective.

The effectiveness of supervision depends on whether: (i) the risks have been anticipated in the project design, which transforms them into operating assumptions, and those are in fact the ones that do arise during execution; (ii) there is an information system with indicators that can anticipate and measure risk, and provide support for monitoring activities, by the deadlines established for the project[47]; (iii) there is a timely response when problems appear, as a result of periodic reviews; and (iv) efforts to overcome those problems are monitored, and that the final execution evaluation will assess the impacts on achievement of the project's objectives.

Within this conceptual framework, supervision is necessary at each stage of the project lifecycle: at the design stage, because of its importance in anticipating risks and planning the set of appropriate supervision instruments for monitoring and evaluation; at the initial stage of execution, because of the need for a proper assessment of program execution capabilities, administrative systems and financial control, as well as providing a results framework for measuring performance against objectives. This stage, which is essentially preventive, reflects the principle that taking early action will have a positive impact on the future of the project.

In the execution process, periodic monitoring instruments are used and they provide the information needed as input for self-evaluation, which identifies problems in the external setting, management risks, ethical issues or problems arising from the operational capacities of the executing agencies or the Bank. They also provide information on progress in achieving the planned products and results. Upon completion of the project, they show how the risks have impacted the project and how the identification and management of those risks contributed to the project's outcome.

Risks occur not only during the disbursement of funds. They can be identified in project design and can continue to exist after the last disbursement. The supervision cycle is organized in light of the assumptions made in advance of the operation, and it includes the subsequent evaluations that report on the attainment of the development objectives and their sustainability.

This supervision model, briefly characterized, requires the simultaneous participation of many players (executing agencies, beneficiaries, the Bank's Country Offices, regional operations departments, auditors, supervisors and external evaluators), who have different roles. Those roles must be synchronized in accordance with an opposing-interests approach

[47] The increasing likelihood of the assumptions occurring or the emergence of new risks presenting grows over time. Failing to meet the deadlines usually exposes a project to uncertainties not provided for in the design.

that underlies the validity of the supervision process. This approach must be established in clear and individual ground rules that set out the sequencing of the instruments used, the products expected of them, their timing, and the responsibility of the people who must participate in them.

Finally, supervision systems are employed for their capacity for monitoring and self-evaluation on the part of project management, but also for the operation of external mechanisms of independent supervision that will confirm the system's functioning, in accordance with the established regulations and strategic objectives established by the organization and the requirements of accountability.[48]

C. Products of the Project Execution Supervision System

1. Background

The Bank's approach to project supervision has been evolving from one based largely on monitoring physical and financial progress to one that focuses on efficiency and the achievement of development objectives.

In the period immediately prior to the Bank's reorganization in 1994, the supervision system was based on annual management reports on portfolio execution for the Board of Executive Directors, with an emphasis on the accomplishment of project objectives.

With the reorganization of the Bank, the basic principle of supervision shifted its emphasis to the responsibility of the regional operations departments (hereafter RE) for administering projects and for reporting that targeted the impact of the outcomes of their objectives.[49] In this way, all matters relating to the actions of project personnel were consolidated under the supervision of the RE.

Within this new regulatory context, a pilot program was developed in 1994 for monitoring project performance, covering one-half of loans in 1995, and the entire portfolio in 1996. At the end of that year the annual portfolio administration report was prepared.

In 1995, Portfolio Review Missions were initiated, led by the Regional Operations Manager or Deputy Manager. Some managers began to request Sector Portfolio Review Missions. The new mandates and the changes in the Bank's lending instruments (sector policy loans, time-slice operations, amendments to investment loans, etc.) tended to increase the requirements for annual and midterm project review missions.

In 1996, the Management Review Committees began to review project completion reports, in addition to the annual country portfolio reviews and the midterm mission reports.

In 1996, a working group report for strengthening the Bank's Country Offices (CO) was approved, reaffirming the primary responsibility of the COs for the administration of

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[48] Evaluating the Bank's supervision activities is a function assigned to OVE in Bank regulations (document RE-238).

[49] These elements were based on recommendations in the TAPOMA report.

project execution, and making them accountable to the RE. That report also proposed a series of recommendations for strengthening the supervision capacities of project management personnel in the COs, in which supervision was taken to mean identifying implementation problems and proposing measures for improving execution performance, in terms of enhancing the project's impact on development effectiveness.

Since 1997 the new project performance monitoring report system (PPMR) has been in place, together with procedures and guidelines for the Project Completion Reports (PCR) and the Loan Administration Missions (LAM). These complement the existing supervision instruments, which have been continuously updated.

2. Description and basic principles

The objective of the SEP is to improve the understanding of the Bank and of its member countries about the status of projects and their performance, to allow for the timely identification of problems and changes in circumstances affecting their implementation, so that corrective measures can be taken to enhance the quality of the portfolio in execution and increase the probability of achieving development objectives.

According to document CP-1283,[50] there are three basic principles underlying the SEP. First, it must be "borrower-linked", i.e. it must be useful to borrowers in managing their projects and in resolving execution problems, as well as being an integral part of the dialogue between the Bank and the national authorities. Second, it must be "Bank-useful", i.e. it must provide relevant advance information on the status of projects for use in preparing the terms of reference for each supervision mission. Third, it must be "cost-efficient" for users, and must be incorporated into a centralized database within the Bank's management information system, in such a way as to facilitate updating, access and the production of reports.[51]

The system is seen as an instrument for helping the various players involved, without detracting from their responsibility for the achievement of objectives, which is considered the key to successful execution.

This view of the SEP underscores the importance of having the Bank and its member countries agree on indicators and oversight activities during the preparation of operations that can be used to assess the achievement of objectives during execution and in the evaluation.

3. Supervision cycle

The supervision cycle corresponds normally to the project execution period. This is identified as the period that begins with the final step in project preparation, normally approval by the Board of Executive Directors, and ends with the project completion report.

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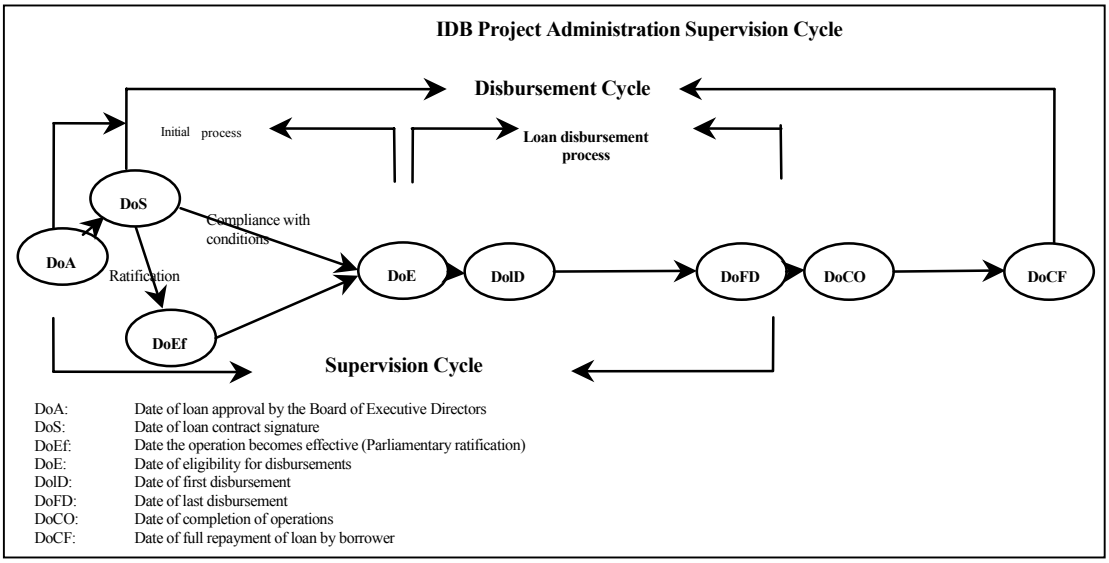
[50] Working Group Report: "Project Supervision and Classification", March 1997.

[51] See document CP-1283.

For purposes of evaluating the supervision system, the relevant cycle for specifying the validity of each of its component instruments relates to the stages of the Bank's disbursement cycle, which is shown in the following graph.



The disbursement cycle begins to run when the project, having been approved by the Board of Executive Directors (DoA), is signed by the borrowing country (DoS). At this point a process begins with three separate stages: the initial process that runs from the country's signature of the loan contract until the date of eligibility for the first disbursement (DoE), which coincides with fulfillment of the conditions precedent. The disbursement process then begins, unfolding in two separate stages: the first extends until the operation is fully disbursed, or date of last disbursement (CDD), and the second runs until the loan is fully repaid by the country.

The execution supervision cycle was defined as the period from the time the project is approved by the Board of Executive Directors until 90 days after the date of the final disbursement. By this date, management must have completed the Project Completion Report (PCR). However, the supervision instruments within this cycle have varying periods of validity or moments of realization. As a result, limits were introduced governing the time that each supervision tool could be used.

This evaluation considered as a relevant part of the supervision cycle, the borrowers' ex post evaluations (BEP) or those that the Bank requires for its own purposes (FIN). This reflects the fact that the project benefits may be produced not only during the disbursement period but also after the project has been completed. This represents an important difference with respect to the criterion used, to the extent that the Bank interprets supervision as referring only to the loan disbursement process.

4. Identifying the instruments of supervision

Application of a broad concept of execution identified 16 different supervision products used by the Bank to ensure proper monitoring of its operations. These instruments are regulated in specific policies and manuals relating to monitoring, support, and evaluation for operations financed by the Bank (OA) and in the policies governing the functions of the Bank's Country Offices (CO).

This identification covers only "products or instruments" of supervision, and therefore excludes the regular activities of CO operations administration (verifying compliance with contractual conditions, verifying and approving procurement, validating and authorizing disbursements, approving amendments to operations, etc.),[52] which are the basic inputs for those instruments.

The instruments considered can be grouped in four broad categories.

The first category consists of **Loan Administration Missions (LAM)**, which are project-specific supervision activities normally headed by operations and technical departments from headquarters. These are designed to assist specialists in the Country Offices with their responsibilities for administering project execution, by providing specialized knowledge for dealing with problems. These missions are of four kinds:

1. **Start-up Missions (OA-222),** normally led by the Project Team Leader, which are used for prior discussion of operational aspects, expected outcomes, supervision parameters and activities, and the necessary capacities of executing units, and to provide consistent support in the transfer of project administration and supervision to the Country Office. Whenever possible, such missions take place in the first month after DoA. They are organized to meet the specific circumstances, or because they are called for in the Project Report or the Operation Plans.

2. **Annual Review Missions (OA-222),** which will be conducted once a year, if called for in the project document, to assess the quantitative and qualitative progress of execution. If they are stipulated in the project document, specific missions will be conducted at the discretion of the Representative or the relevant divisions.

3. **Specific Missions (OA-222)** are intended to address unresolved issues and problems that require special attention.

4. **Midterm Review Missions (OA-222)** are conducted in accordance with the modality of the operation, or when circumstances so require, or where such missions are stipulated in the Project Report or Plans of Operations. Their purpose is to evaluate project execution, verify major achievements and

[52] See OP-306 and CO-204 for actions that were considered activities concurrent with products of the supervision process identified for the evaluation.

problems, assist in finding solutions to problems and, if necessary, to reformulate the operation.

The second category of supervision instruments consists of the **Portfolio Review Missions**, led by the Regional Operations Departments (RE), for the review of operations in execution. Such missions are of three kinds and respond to different needs:

1. **Annual Portfolio Review Missions (OA-223),** generally led by the regional manager or deputy manager, are conducted once a year for discussion with the executing agencies and the country authorities about general aspects of the portfolio (fiduciary, socioeconomic, political and institutional), the specific aspects of each operation, project by project, including a review of compliance with contractual conditions, and the achievement of development objectives, and to decide on actions, timetables and responsibilities for improving execution and achieving goals. The outcome of the missions will be taken into account in preparing the annual portfolio report for the Board of Executive Directors.

2. **Sector Portfolio Review Missions (OA-224)** led by the corresponding division chief, have similar objectives to the foregoing, but relate to the portfolio in a specific sector. They are conducted at the discretion of the Country Office or the division.

3. **Annual Portfolio Evaluation (OA-230/CO-302).** Every CO is responsible for preparing this year-end report, with the participation of local authorities and borrowers. They are intended to provide a quantitative and qualitative evaluation of country portfolio results (investment projects and sector loans only) covering general aspects of projects in execution as well as the prospect that they will achieve their development objectives. These reports serve as basic input in preparing the Annual Report on Projects in Execution (ARPE), which is produced at headquarters by ROS for submission to the Board of Executive Directors.

The third category consists of the **supervision instruments used by the Bank's Country Offices**, for which they are accountable to the RE. They are of six kinds:

1. **Technical Inspection Visits (CO-204/CO-308)** are intended to determine the current status of technical, economic and environmental questions concerning a project (loan, technical cooperation and small projects), and the extent to which development objectives are being achieved. They are the primary responsibility of the sector specialist and must follow an annual plan of the CO, resulting from an exhaustive process of risk assessment, updated on a quarterly basis. While the frequency will depend on the circumstances of the project, the program must include, as a minimum, an annual visit to the executing agency and a visit to the project site, using selective criteria. The results must be reported to the executing agency.

2. **Institutional and Financial Inspection Visits (CO-204/CO-308)** have objectives similar to the foregoing, but refer to compliance with the financial conditions of the contract, the project's financial performance, and the institutional structure of the agency responsible for the project's financial and accounting management. These visits are the responsibility of the financial specialist and, if necessary, the sector specialist will participate. They are planned to respond to circumstances relating to risk, and do not have to be conducted annually. Financial statements and the reports and recommendations of external auditors are an essential input for these visits. Their results must be reported to the executing agencies.

3. **External Audits (OA-419/AF-100/AF-200/AF-300/AF-400/AF-500)** are intended to provide an independent audit of the financial administration of each loan during its execution period (Bank funds, local counterpart funding, and other financing), from the time disbursements begin until the funds are totally disbursed. No audit is required in the fiscal year in which the contract is signed. The COs are responsible for overseeing compliance by borrowers and executing agencies with the contractual commitments relating to external audits. When those audits detect serious problems, action must be taken immediately to correct them.

4. The **Project Performance Monitoring Report (CO-303)** is the main tool for supervision and self-evaluation of project execution. It is designed as an oversight mechanism for project execution and the achievement of development objectives. It must identify the risks to project implementation and recommend corrective measures for addressing them. Consistent with the Bank's interest in the outcome of operations, it also requires staff to issue an opinion on the probability of achieving the development objectives, on the progress of implementation, and on the validity of the project's design, as well as on external influences (assumptions). This supervision tool is prepared by the CO and provides input for other supervision instruments (such as the CPR, the LAM, the APE, the PCR, the PAIS and the BEP or FIN), while drawing upon other inputs (such as project design and inspection visits). These reports are required as of the operation's DoA, and the Representative officially approves their content twice a year (by 30 June and 31 December).

   The PPMR system is based on the logical framework methodology and is used to classify the achievement of development objectives during the execution of each project, by measuring in advance the probability of success upon completion.

   The probability that development objectives will be achieved depends: (i) as a necessary condition, on the probability that the progress of implementation will lead to successful completion of project components in terms of quantity, quality, timing and cost efficiency; and (ii), as a sufficient condition, on the probability that the key assumptions identified in the design or execution will hold true. If this is not the case, the development objectives may not be achieved

even if the project is completed as planned. The validity of the assumptions affects the feasibility both of the outcomes and of the development objectives.[53]

5. The **Project Completion Report or PCR (CO-309)** is the final product that management uses for project execution supervision (only for investment projects and sector loans, generally) and it is in turn a key element of the Bank's evaluation system. It provides the necessary information for improving the identification, design, analysis, approval, execution and quality of the policies and procedures of future projects. It is the responsibility of the sector specialist to prepare the report within three months after the final disbursement, and it is reviewed by the Representative. The sector specialist may consult Headquarters personnel or specialists assigned to the project, and may encourage borrowers, beneficiaries and executing agencies to participate in its preparation. The regional manager is responsible for verifying terms and deadlines and deciding whether review by the CRG is required.

6. **Ex Post Evaluation of the Borrower (CO-205).** The CO supervises the borrower's work in preparing the BEP, when applicable (the loan contract makes this voluntary, at the option of the borrower), following conclusion of the project (only for investment projects and sector loans). The objective is to evaluate the degree to which the project's goals, objectives and socioeconomic impacts have been achieved, and to propose strategies for improving projects. The work of preparing the BEP must generally begin within three years after the last disbursement.

7. **Final Bank Evaluation (CO-205).** If the borrower decides not to conduct a BEP voluntarily, the Bank may, for its own purposes, require a final evaluation, in which case it will be responsible for defining the approach, its cost and financing.

The fourth category of supervision instruments relates not to specific Bank policies but to the **supervision systems or functions** assigned to central departments at headquarters. They are of two types:

1. **Project Alert Identification System (PAIS).** This is an additional tool for project execution monitoring, assigned to ROS/PMP, to complement performance information currently provided in the Project Performance Monitoring Reports. Projects on alert status are those that, while they may be making adequate progress in achieving their development objectives, are classified in the PPMRs as unsatisfactory or highly unsatisfactory in light of poor implementation progress reports or a low probability of assumptions holding true, or that manifest one or more indicators of potential problems, from a set of eight indicators relating primarily to disbursement. This group of

[53] Adverse risks transformed into favorable risks (i.e. from the viewpoint of their mitigation) are converted into project assumptions, which must hold true until the end of the execution period in order to achieve the project's development objectives.

projects is distinguished from normal projects and from problem projects, which are those with little likelihood of achieving their development objectives, regardless of their implementation progress classification and the assumptions underlying them.

2. **Administrative and Operational Review of Country Offices by the Auditor General (OR-AUG)** is an activity performed in a decentralized way by the Office of the Auditor General, at the request of the Office of the President, in accordance with established procedures, to review and evaluate the effectiveness of financial and operational administration in the Country Offices, examining compliance with Bank policies, standards, plans and procedures, and making recommendations to correct shortcomings or weaknesses, and advising management of the risks of not adopting them. This external supervision activity is performed in each CO, normally every two years.

D. Characteristics of the Project Execution Supervision System

The Bank's supervision system sets a "minimum level" of products to be supervised, which is the level established as mandatory in its policies. The instruments included in this minimum are: the Annual Portfolio Review Missions (CPR), the Annual Portfolio Evaluation by the COs (APE), the Technical and Financial Inspection Visits (IVT and IVF), the External Audits of Loans (EFA), the PPMR and the PCR. The remainder of the supervision products are considered mandatory if the project document so stipulates. In this category are Loan Administration Missions (LAM) headed by the Regional Operations Departments (MS, MA, MSP, and MMT) and the ex post evaluations (BEP and FIN). Even if not included in the projects, these activities may be conducted if circumstances during implementation so warrant.

The supervision instruments for each phase of the project execution cycle are a single instrument (MS) for the initial stage; three instruments (PCR, BEP and FIN) for the project completion phase, of which only one (PCR) is compulsory according to Bank policies, where beneficiary participation is voluntary. All other instruments of supervision (11 instruments) focus on the disbursement cycle, in which six of the seven supervision instruments mandated by Bank policy are applied.

Outline of the Bank's Project Execution Supervision Model													
Supervision Instruments	**Acronym**	**Based on type of supervision**					**Based on stage of execution cycle**			**Based on compulsoriness**		
			Self-evaluation		**External evaluation**							
		Project supervision	**Projects**	**Project portfolio**	**Appropriate use of funds**	**Achieve objectives**	**Start-up**	**Process**	**Completion**	**Mandatory by policy**	**Required by project**	**Other**
Loan Administration Missions												
1. Start-up mission	MS	*					*				*	
2. Annual review mission	MA	*						*			*	
3. Specific mission	MSP	*						*			*	
4. Midterm review mission	MMT	*						*			*	
Portfolio Review Missions												
5. Annual country portfolio review mission	CPR			*				*		*		
	SRM			*				*				*
6. Sector portfolio review mission	APE			*				*		*		
7. Annual portfolio evaluation												
Country Office Instruments												
8. Technical inspection visits	IVT	*						*		*		
9. Financial inspection visits	IVF	*						*		*		
10. External audit	EFA				*			*		*		
11. Project performance monitoring report	PPMR		*					*		*		
12. Project completion report	PCR		*						*	*		
13. Borrower ex post evaluation	BEP					*			*		*	
14. Bank final evaluation	FIN		*						*		*	
Functions assigned to HQ Departments												
15. Project alert identification system	PAIS-ROS		*					*				*
16. Operational/administrative review of Country Offices	OR-AUG				*			*				*

Depending on the type of supervision, the Bank's system has the following special features: six of the 16 supervision instruments (the four LAMs and the two kinds of inspection visits) are for project execution monitoring; a further seven instruments focus on self-evaluation, four at the project level and three for all or part of the portfolio; and three instruments are for external evaluation: two are used to oversee the appropriate use of project funds, and one to evaluate fulfillment of objectives and project impact.

While this characterization refers exclusively to the "minimum compulsory" instruments required under Bank regulations, it is important to note that, project monitoring is only mandatory in the case of inspection visits. Self-evaluation combines five of the seven mandatory instruments. For external evaluation, only the annual external audits of loans are mandatory.

To conclude, the Bank's execution supervision model establishes a "compulsory minimum level" that includes fewer than 50% of the instruments identified (seven out of 16). This minimum level focuses basically on supervision of project execution processes. Their use during the initial or post-execution cycles is voluntary.

With respect to supervision of performance evaluation, the mandatory instruments focus on self-evaluation and in audits on proper use of disbursements, but not on the way those funds contribute to the purposes for which they were granted. The supervision system basically centers on reducing risk in the handling of project disbursements.

This evaluation will take this characterization into account, by testing the degree of compliance with this "minimum level" during the period under review; observing whether the supervision activities actually conducted diverged from this minimum, by means of the particular instruments specified for each project; and, finally, verifying whether supervision was consistent with risk management.

THE DURATION OF PROJECT EXECUTION AND ITS RELATIONSHIP TO SUPERVISION

This Annex examines the duration of project execution, the different activities involved throughout the process, and the way it influences supervision.

For purposes of empirical analysis, all projects that were eligible during the period 1998-2001 were considered. They were divided into two universes: policy-based loans (PBL) and other loans. These two categories involve differing initial conditions for their programmed execution times. The total number of projects in the sample was 529, of which 42 are PBLs.

The total execution period, from approval until the actual date of last disbursement (established at 31 December 2001) was divided into stages corresponding to the various supervision dates: those relating to the startup process (date of signature, effective date of contract, and date of eligibility) and those relating to the disbursement process, distinguishing the original date set for last disbursement (ODD) and the actual date of last disbursement (CDD).

Project Execution Period, 1998-2001

Number of months from date of approval (DoA)	Loan execution period, excluding PBLs (months)	PBL execution period (months)	Loans excluding PBLs		PBL loans	
			% by CDD	% by ODD	% by CDD	% by ODD
Date of signature (DoS)	5	3	6.4	8.9	6.0	8.8
Effective date (DoEf)	7	5	9.0	12.5	10.0	14.7
Date of eligibility (DoE)	15	8	19.2	26.8	16.0	23.5
Original date of last disbursement (ODD)	56	34	71.8	100.0	68.0	100.0
Actual date of last disbursement (CDD)	78	50	100.0	140.0	100.0	147.1

Average number of years of execution	6.5	4.2
Average time overrun (months)	22	16

The average execution time of projects is 6.5 years for loans other than PBLs, and slightly more than four years (50 months) for PBLs. This implies an average overrun against the originally planned completion date of 22 months and 16 months respectively, or nearly 50% of the originally planned time limits. Taking the CDD as the baseline, the initial process, from DoA to DoE, accounts for 19% of non-PBL project execution times (15 months) and 16% of PBL execution times (eight months). Taking the ODD as the baseline, these times are 27% and 24%, respectively.

These overruns indicate that the average values for the Bank, in particular for non-PBL projects, are very close to two of the parameters that are used in the PAIS for identifying projects at risk. Those two parameters are: (i) the delay in achieving eligibility is 12 months or more from the effective date, and (ii) projects requiring extensions of 24 months or more for the date of last disbursement.

The Bank's average situation is different if one looks at data for the three regions. Region 1 shows the best performance in execution times, under both categories of loans considered. For non-PBL projects, the percentage impact of initial processing and disbursement processing times is similar in the three regions. The situation changes for the PBLs, where the initial process shows a clear difference between Region 2 and the other two regions, reflecting the impact of the delay in the effective date of the projects (parliamentary ratification); this initial delay tends to be made up during the disbursement process.

The average delays in months for non-PBL projects in Region 2 and Region 3 are virtually the same as the PAIS risk parameters.

Project execution duration indicators: 1998-2001 (by Regions and Total)

Bank	Initial process [1/]					Disbursement process [5/]					
	Months	Signature (% by CDD) [2/]	Effectiveness (% by CDD) [3/]	Eligibility (% by CDD) [4/]	Total (% by/CDD)	Months	% CDD/ODD (after DoA) [6/]	% CDD/ODD (after DoE) [7/]	Physical and financial progress [8/]	Total (% s/CDD)	Months
Loans excluding PBLs											
Region 1	14	6.0	2.0	10.0	18.0	61	134.0	145.0	1.26	82.0	75
Region 2	16	7.0	4.0	9.0	20.0	62	142.0	159.0	1.23	80.0	78
Region 3	17	8.0	0.0	11.0	19.0	65	144.0	160.0	1.34	79.0	80
Total Bank	15	7.0	2.0	10.0	19.0	63	140.0	154.0	1.27	81.0	78
PBLs145.0											
Region 1	4	2.0	3.0	6.0	11.0	35	145.0	154.0	0.48	89.0	39
Region 2	15	11.0	8.0	9.0	28.0	38	137.0	160.0	1.33	72.0	53
Region 3	6	5.0	0.0	6.0	11.0	49	155.0	166.0	1.08	89.0	55
Total Bank	8	6.0	3.0	7.0	16.0	42	146.0	161.0	1.12	84.0	50

1/ Period running from date of approval by the Board of Executive Directors (DoA) until first disbursement.
2/ Months from DoA to DoS/months from DoA to CDD *100
3/ Months from DoS to DoEf/months from DoA to CDD *100
4/ Months from DoEf to DoE/months from DoA to CDD *100
5/ Period running from date of first disbursement (ID) to final disbursement
6/ Months from DoA to CDD/months from DoA to ODD *100
7/ Months from DoE to CDD/months from DoE to ODD *100
8/ Months of execution from DoE/months of disbursement execution from DoE (excluding projects completed in 1998-2001)

Note: Countries requiring prior parliamentary ratification for project effectiveness are:
Region 1: BO, CH, PR;
Region 2: CR, DR, ES, HA, HO, NI. In GU, the contract is signed upon parliamentary ratification.
No countries in Region 3 have this requirement.

These time overruns are associated with a greater likelihood of circumstances leading to nonfulfillment of the project's original objectives, reduce the net present value of its benefits, and occasion greater costs to the country. These overruns involve an opportunity cost for funds that could be used for other purposes, increase the impact of risks in the project cycle, expose more projects to the uncertainties of the domestic political cycle,

increase the likelihood of shifting priorities, raise the possibility of project reformulation or cancellation, and lower the net present value of the project benefits.[54]

In this context, it also becomes necessary to expand periodic supervision activities beyond what has been planned, by either prolonging the time-frame itself, or addressing a setting of increased risk, depending on the situation. This raises the cost of supervision, adds to the financial costs of operations (fees and interest), and augments the size of annual amortization installments, through a shorter loan repayment period.[55]

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[54] Similar concerns are indicated in document GN-2215-1, Portfolio Management Action Plan, 6 February 2003, paragraphs 2.06 and 2.07.

[55] As of 2003, execution delays will not trigger automatic extensions in the project grace period, in which case countries may find themselves starting to repay the loan principal before the project's benefits have been realized.

THE IMPACT OF THE USE OF SUPERVISION INSTRUMENTS ON DEVELOPMENT RESULTS

This chapter discusses the extent to which supervision activities programmed and conducted by the Bank were important in monitoring of output performance. This aspect will be analyzed from two viewpoints. First, the chapter examines the use of supervision instruments for supervision of the results of operations in 1998-2001. It then considers the use of supervision instruments that involve formal participation by the borrower in the planning, execution control, and evaluation of projects.

A. Supervision of project outcomes

The importance attached to supervision of outcomes is measured by the degree of compliance in the use, together with borrowers, of key instruments for identifying and confirming results at various stages of the project cycle: at startup (MS), during execution (MMT) and upon completion (FIN and BEP).

The importance of supervision linked to outputs evaluation

Concept	No. of projects with activities:								
	Programmed			Programmed and executed			Executed (programmed and non-programmed)		
	MS	MMT	FIN/BEP	MS	MMT	FIN/BEP	MS	MMT	FIN/BEP
1998-2001	17	200	52	3	20	20	77	46	22
Representativeness (%)	5.4	57	37.4	1	5.7	14.4	24.5	13.1	15.8

Note: Representativeness was calculated with respect to the projects for which such activities could have been conducted during the period.

The indicator used to measure the magnitude of supervision outcomes with borrowers is the ratio of the number of activities planned and executed to the total number of potential projects in which such activities might have been conducted in 1998-2001.

The results show that for two of the instruments (MMT and FIN/BEP) programming was significantly more important than execution. In the case of the MS, the results are the opposite. In terms of the representativeness of these programming instruments, MS was planned in 5% of projects, MMT in 57% and FIN/BEP in 37%. When applied to supervision activities actually conducted, the corresponding figures are 25%, 13%, and 16% respectively, indicating that more MS are conducted than planned, while the reverse is true for the other two instruments.

To conclude, then, supervision instruments are not used much to evaluate outputs, other than those results from self-evaluation. In fact, such instruments are programmed for only one third of all projects, and actually used in only 15% of those projects. The performance of MS is somewhat better than programmed, but starts from very low initially planned levels. The MMTs, which are used for monitoring the results during execution, are important because of their capacity to pinpoint potential problems in advance. They are actually conducted, however, in only 13% of possible cases. These results show that the Bank monitors the achievement of results primarily through self-evaluation instruments, such as the PPMR and PCR, in which participation by borrowers and beneficiaries is either not provided for, or is voluntary.

B. Supervision linked to dialogue with the borrower

One of the basic operating principles of the Bank's supervision system is to have a system that strengthens dialogue with the borrower and borrower participation. To this end, evaluation focuses on the degree of compliance in the use of six supervision instruments considered most closely linked to formal dialogue with the borrower ("borrower-linked") during the period. This group of six instruments, which introduce formal input from executing agencies, consists of MS, MA, MMT, CPR, PCR, FIN, and BEP.

Importance of borrower-linked supervision, 1998-2001

Concept	No. of supervision activities						Total
	MS	MA	MMT	CPR	PCR	FIN/BEP	
Activities programmed	17	244	200	1,679	132	52	2,324
Programmed activities executed	3	115	20	1,306	120	20	1,584
Activities executed (programmed and non-programmed)	77	361	46	1,306	120	22	1,932
	Representativeness (%)						
Programmed:	5.4	17.6	57.0	100.0	100.0	37.4	58.0
Programmed and executed:	1.0	8.3	5.7	77.8	90.9	14.4	39.6
Total executed:	24.5	26.0	13.1	77.8	90.9	15.8	48.3

Note: The degree of representativeness is the ratio between activities programmed or executed and the total of possible supervision activities that could have been conducted during the period.

Borrowers do not have the same degree of involvement in these instruments. While four of them call for participation by executing agencies, participation in the PCR is voluntary, and preparation of the BEP is the responsibility of the borrower. Moreover, five of the instruments relate to project dialogue, while the CPR is used in the annual discussion of the

country portfolio in execution. Despite these distinctions, the instruments are designed to measure the degree to which borrower viewpoints are taken into account in supervision.

The indicator that measures the representativeness of these instruments is the ratio of all supervision activities programmed (or executed) with the six instruments to all possible supervision activities that could have been conducted during the period.

The results show that borrower-linked supervision activities were planned in 58% of possible cases, a figure that falls to 40% when applied to programmed activities that were actually conducted. Considering the total of activities conducted, including those that are compulsory and those that are established voluntarily, the importance of borrower-linked supervision rises to 48%, reflecting the increase in unprogrammed MS, MA, and MMT activities.

The supervision tool most widely used for purposes of Bank-country dialogue was the CPR, which was used in 78% of all possible activities. This tool has in fact become the key instrument for discussing with the country the risks and problems of the entire portfolio of projects in execution.

In conclusion, it emerges that while borrower-linked supervision activities are on the rise, the level is still well below potential, focusing mainly on the CPR. The CPR has become the main periodic mechanism of dialogue for eliminating risks in the way to attaining project objectives. This tool normally relies on input from the last PPMR of the projects. Considering that executing agency participation in the PCR is voluntary (there is no available information to indicate the degree of actual participation by beneficiaries in the PCR), it is possible that the effective level of borrower involvement is even less.

THE SUPERVISION INSTRUMENTS FOR ASSESSING DEVELOPMENT RISKS DURING PROJECT EXECUTION

A. The Project Performance Monitoring Report System (PPMR)

The Bank's basic tool for managing development risks in project execution is the PPMR. This supervision mechanism reports and monitors problems and risks identified in project design, and those reported by the COs during execution. Based on this, and on an analysis of implementation quality, the PPMR provides value judgments about the probability that a project will meet its development objectives during execution, and the products for achieving those objectives. The PPMR also reports on continuity solutions to anticipate problems, or to mitigate them when they appear. It has become the mechanism for monitoring how the solutions adopted resolve the risks. These aspects must be reported upon completion in the PCR.

In short, the PPMR is a mechanism that, besides assessing the extent to which project assumptions hold true, issues a judgment as to the probability of success in achieving the project's development objectives.[56] Risk supervision through PPMR is the basis for managing the shifting conditions involved in execution, and the way impacts are mitigated.

As a result of the COs' work with the PPMR, the Bank's project portfolio[57] is classified by degree of risk into: (i) Normal Projects, which are those classified as likely to achieve their development objectives (probable or highly probable), where there are no significant implementation problems (satisfactory or very satisfactory), and where key assumptions are very likely to hold true; (ii) Problem Projects, which have little likelihood of achieving their development objectives (low probability or improbable), regardless of implementation progress or fulfillment of key assumptions; and (iii) "At-Risk" Projects, which are projects that, while they can be expected to achieve their development objectives, entail problems with execution or assumptions that point to problems in the future.

B. The Project Alert Identification System (PAIS)

More recently, through the Regional Operations Support Office (ROS) in the Portfolio Management and Project Monitoring Office (PMP), the Bank has developed an additional project monitoring tool, as an adjunct to the PPMR, known as the Project Alert Identification System (PAIS). This system redefines the warning system by adding to the PPMR's "red flag" procedure an "at-risk" classification for projects that, while classified as normal, present two or more of a total of eight potential implementation risks. Those indicators are designed as standard parameters, in an effort to introduce independent and objective criteria.

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[56] The present evaluation deals only with this aspect of risk management. OVE is currently conducting a detailed study to evaluate the treatment of Bank assumptions.

[57] A similar analysis can be made by country, region, sector, type of project, etc.

Of those eight parameters, four refer to disbursement delays following eligibility, three refer to startup delays before the first disbursement, and one refers to lateness in the submission of externally audited financial statements. Thus, seven of the indicators identify excessive delays in initiating disbursements, or disbursements proceeding at a pace other than planned, as symptoms of development risks. The remaining parameter is an indicator of the periodicity of compliance, and not the degree of confidence that funds will be used appropriately, because it does not refer to the quality of their use.

This system sounds warnings relating to the accomplishment of development objectives, by inferring risks from indicators based on the difficulty in predicting disbursement dates for Bank projects. The virtue of these indicators resides in the fact that because they are automatic, they avoid all subjectivity and provide information on opportunity costs resulting from delays in the use of funds. By definition, these indicators do not provide information on the development objectives achieved as a result of disbursements. In this sense, they constitute supplementary input for the assessment issued in the PPMRs, which in the final analysis is the tool used to rate a project's development risk.

Box 3. Complementary indicators.
At-risk projects - PAIS

1. Disbursement period >= 3 years, with less than 25% disbursed.
2. Disbursement period >= 5 years and between 25% and 75% disbursed.
3. Period to initial eligibility (from DoS) >= 12 months.
4. Project with < 10% of initial balance disbursed in last 12 months, eligible >= 3 months.
5. DoS >= 11 months, if no ratification required (from DoS).
6. DoEf >= 17 months, in countries that require ratification (from DoS).
7. Disbursement period extension >= 24 months after ODD.
8. Delay >= 6 months in submission of EFA.