

## Chapter 4.

# Contracting out Core Government Functions and Services in Afghanistan

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Seema Ghani and Nematullah Bizhan

### Abstract

This chapter explores a number of examples of contracting out in Afghanistan. The lessons elaborated in this report stem from a number of sectors, including finance, aid effectiveness and justice. Several important recommendations are drawn, which can support other post-conflict and fragile states to strengthen the delivery of government services to their citizens.

### Executive summary

After 30 years of war and conflict in Afghanistan, we are noticing some progress in the public sector. In 2002 the interim government inherited a broken system with bare-bones infrastructure: offices were without chairs and tables, and there were certainly no electronic devices such as computers. With such a low starting point, the international community and expatriate Afghans had high expectations. There was an unrealistic hope that the interim government would fix everything in a matter of months.

With the weak civil service, administration and management and a non-existing information technology (IT) infrastructure, the government had to either fully or partially contract out certain functions. Many of the contracts did produce a return on investment, for example in finance, banking, trade, police and the military. Yet many government institutions have continued to struggle to put together a workable mechanism and process. These include the judiciary, education, public transport, agriculture, energy and water, and infrastructure building.

After seven years, the government of Afghanistan is still struggling with its daily functions and operations. Corruption is more prevalent than ever in such a fragile situation. But on the other hand, the building blocks of some of state functions have been put in place, such as the financial management system.

Overall, we found that there are some success stories in contracting out government functions, as well as some less successful experiences. We draw on our analysis to make the following general recommendations:

- ▶ Assessing the need for contracting out experience is key before deciding to contract out a function. Some functions can work through internal consultants or by hiring temporary consultants that can perform the function in-house.
- ▶ Ownership and capacity building should work together in any contracts. While the function may be contracted out, the government should not forget to plan an exit strategy for the contractor so that the government can take over the function at some point and be able to rely on its own capacity.
- ▶ There are certain functions that the government can and should contract out over the long-term; one example in Afghanistan is the health sector. The success rate of NGOs and private hospitals is high in delivering good services; policy makers should consider keeping this function under the purview of outsiders.
- ▶ In the process of contracting out, one should use local capacity as well as international capacity. Using locals builds their capacities so that in the future these services can be provided at a lower price.
- ▶ Consider contracting expertise from within the region. A region with a similar cultural connection and background to Afghanistan can bring added benefit. India is a good example of a source of similar experiences in many sectors, if not all.
- ▶ Co-ordination is needed amongst stakeholders. The government, the donor community and the contractor should all be reading from the same page. A third party, such as the people's representative or the parliament, could get involved in countries where the government has low capacity or is not accountable. In Afghanistan corruption can be high where large contracts are in operation.

## Introduction

This study lists a number of government functions that have been either partially or fully contracted out in Afghanistan. Most of these functions are core to the everyday running of public services. An example is financial management through the Ministry of Finance. When the new government took over in November 2001, the ministry was not functioning well. The budget was so small that it couldn't meet even the most basic needs. Building a state costs money and handling money requires clear accountabilities and efficient processes. The donor community was prepared to pay for setting-up the processes, but the system lacked experienced staff. In some areas where there were human resources, creative management was lacking.

Some of these core functions of the government, therefore, had to rely on help and advice from international organisations. This became a theme throughout government, and continues to be so in Afghanistan. Afghanistan became the "land of opportunities" for adventurous international workers. It became useful to have an "Afghanistan experience" on one's CV in order to get better jobs elsewhere. Contractors such as Louis Berger, BearingPoint and Adam Smith International (ASI) have been major players in delivering government services.

This study aims to give examples of both success stories and failures in contracting out, and to analyse the underlying reasons. We also list some lessons learned and make recommendations for future success. It is hoped that these recommendations will be adopted in Afghanistan in the near future.

The paper is based on the authors' personal experience, as well as on some documented material. Seema Ghani is the former Director General of Budget and Nemat Bizhan has budget management experience, as well as experience with the Afghanistan National Development Strategy. We also interviewed some of the parties involved to fill gaps in our knowledge base. Exact quotes have not been used, but the names of the interviewees are listed in Annex I.

## **An overview of contracted out projects in Afghanistan**

In the past few years, the donor community has invested money in Afghanistan to set up a legitimate and functioning government accountable to its people. This support included help with handling/managing money, building or renovating offices, running the administration and many other areas where previous governments had failed to manage. Most existing functions needed to be reformed; other basic functions needed to be created after decades of war. Some donors' assistance involved contracting their own consultants and seconding them to the government. Other donors took responsibility for setting up the entire function until it was ready to hand over to the government. This section introduces some of the core functions of the government that were either fully or partially contracted out to external actors, such as the World Bank (WB) consultants, United Nations Development Program (UNDP), other UN agencies, NGOs and private companies.

### ***Afghanistan Reconstruction Trust Fund (ARTF)***

The World Bank took administrative and financial responsibility for this fund in 2002, initially sharing management responsibility with UNDP, the Islamic Development Bank and the Asian Development Bank. This fund created a suitable mechanism for donors to resource the operating budget and major projects under the development budget. Pledges totalling USD 59 million were received for 2002/03 from eight donors, the largest of which were from the Netherlands, Germany, Italy, UK and Denmark. The donor community needed a system to facilitate accountability and transparency. ARTF happens to be one of the most successful mechanisms so far, despite its bureaucratic processes. Although there are still some problems with the way the fund is managed and operated, the WB has been able to manage it successfully. Lack of experience meant that the government of Afghanistan was unable to manage it. Had the level of corruption been lower and had adequate staff been trained, this fund would have been handed over to the government by now. One of the biggest failures of the international community and the political leaders of Afghanistan has been the lack of effective capacity-building programmes. Eight years later, the country is still buying in capacity at a very high cost without much focus on programmatic capacity development. As a result, ARTF remains a fully outsourced project in Afghanistan.

### ***Ministry of Finance and Ministry of Commerce legislative drafting***

Financial and commercial functions, such as income tax policies and related laws, budget law, procurement law, revenue related regulations, trade policies and many others would not have been possible to draft without contracting in experts from companies such as BearingPoint, Adam Smith International (ASI) and UNDP. This contracting started in 2003 and in some areas still continues. ASI and BearingPoint were two of the first companies that were contracted to take responsibility in various areas of the ministries of finance and commerce, mainly to write legislation. Experts were needed to bring their experience of other countries to write or amend the Afghan legislation. This was best managed and run by the international companies whom the donors could trust. Most of the contracts that BearingPoint won were funded by USAID; ASI, being a British company, was appointed by the UK Department for International Development (DFID).

### ***Treasury reform***

This included setting up an automated national payroll system/decentralised payroll system, the Afghanistan Financial Management Information System (AFMIS), and accounting. These functions were assisted through a BearingPoint contract with USAID funding. The accounting system contract was funded by the WB, although this also was contracted to BearingPoint. They started in September 2002 and continued into planning and design phases in 2003. The decentralised payroll system has

been one of the most successful projects: corruption has been reduced by automating the payroll and an automated system has also improved banks' performance since their services were also required. Most banks had not been functioning properly previously. There were numerous ghost employees in Kabul and in the provinces; the automated system reduced their numbers. Six years on, fewer people are able to misuse the payroll system. Additionally, government employees in most parts of the country now receive their salaries on time. The system, however, has not completely solved all the problems. Poor security means that some people in the provinces still do not always receive payments on time. On the whole, however, the achievement of a functioning system of payment gets closer every day.

At the same time as the payroll system was installed, an automated system for issuing electronic cheques was also contracted to BearingPoint. This contract was operated by a team of international and national consultants. These facilities in the Ministry of Finance and the central bank would not have existed without being contracted out to an experienced international company. BearingPoint has managed to win many contracts in financial management in Afghanistan since 2002. One reason is that they were already present and able to convince the two main donors, WB and USAID, that costs would be lower if they were granted other contracts.<sup>72</sup>

If such projects had been fully managed by the ministry while recruiting international consultants then progress would have been much slower as senior managers were overloaded. Outsourcing and the assistance of companies in managing some of the projects has made progress possible. The quality of the companies involved is another matter, however, but this falls outside the scope of this study. As stated before it is mainly the donors who are responsible for selecting the companies. Afghan senior managers can only advise; with organisations like USAID, the final decision is solely theirs to make, not the Afghan government.

### **Setting-up the Aid Co-ordination Unit**

This unit is mainly run by consultants hired through ASI and UNDP administrative support. The Ministry of Finance, which houses this unit, is still unable to fully take over this function. Over 70% of the unit's staff is still contracted to ASI and UNDP. Although the manager reports to the Director General of Budget, he is paid by donor funds through UNDP. Other international staff are recruited and managed by ASI. As with other outsourced projects, although the management reports to Afghan supervisors, the supervisors themselves report to the company which hired them. This means that the manager's loyalty is with the company that pays his salary. Most staff contracts state that staff must report first to the company that hired them, rather than to their line manager in the host government. There have been cases of conflict of interest when a member of staff's loyalty has been questioned when he/she has tried to obey the orders of the Afghan institution's manager (for political reasons, the actual example cannot be printed here).

### **The reform of the Customs and Revenue Departments**

This Ministry of Finance reform began in 2002 through international contractors, including a team of Afghan consultants hired by international companies. The WB also agreed to pay for the customs and revenue reform project as part of its contribution to Afghanistan's reconstruction. The old system of customs clearance – which required 25 different forms and the signatures of over 25 officials – was simplified into a single administrative document. Under the previous system, each signature was an opportunity to collect a bribe. Re-engineering and simplifying administrative processes have therefore helped increase efficiency and reduce corruption; a tribute to the contracting agencies.

Revenue policies were also formulated with the help of advisors and partly through a project of reform contracted to private companies such as ASI and BearingPoint. Another important step was the creation of the Large Taxpayers' Office to increase internal revenue. A centralised revenue system was also established in the same manner. Customs offices around the country were obligated to transfer all revenue collected to the central bank account. This controlled corruption stemming from revenue collection in the provinces.

### ***Afghanistan National Development Strategy (ANDS)***

This project began as the Interim Afghanistan National Development Strategy (I-ANDS) in 2005. Afghanistan was not included in planning the UN Millennium Development Goals (MDG) in 2000 because of the Taliban regime. It was therefore hoped that in 2005 – through I-ANDS – Afghanistan could develop a proper poverty reduction strategy to meet the MDG goals. The WB became the lead donor and recruited the first national and international consultants. The government did not have the capacity to run such a unit and so the project was contracted to a group of individual consultants managed by UNDP and funded by the WB, DFID, the Canadian International Development Agency (CIDA), Norway and the Netherlands. This unit was run out of a non-government office and reported to the Senior Economic Advisor to the President. The manager was an Afghan recently returned from studying in the United States. He started negotiating with the WB to recruit international consultants whose appointments both the WB and the administering body (UNDP) agreed. The positions were advertised internationally and the recruitment process began under this manager's guidance. As is common in Afghanistan, however, some consultants did not perform well in the poor security situation; cultural issues, the competitive environment and tight deadlines were also very difficult for some consultants to deal with. Inevitably some contracts had to be terminated as a result.

Staff were employed under various international and local contracts; while some were paid through UNDP, other donors seconded their own staff to the mission. This project had several layers of management, including a manager, a director, and a senior advisor to the president who was in charge of this project. There were also an external advisory committee and a government observer committee. After having completed the initial phases and writing the document, ANDS has now split into two departments under the Ministry of Economy and the Ministry of Finance. The co-ordination function sits within the budget department of the Ministry of Finance, while the monitoring and evaluation department has now moved to the Ministry of Economy. These units, however, are still paid externally through the UNDP office and all financial matters are handled by the UNDP. The directors of the two units are paid through a government budget for high-level jobs and their salaries are very competitive, while the rest of the unit (mainly national consultants and a small number of expatriates) are all paid through UNDP and the donor community fund. Although the work will now belong to the government, it is still partially contracted out – if not fully outsourced. This is because the manager is Afghani and staff report to him rather than reporting only to UNDP and the relevant donors. Just as with the budget team, there may be a transition planned at some point, but for now UNDP will be administering the project with the co-operation of the two Afghan directors. Currently a team of UNDP experts is working on setting up an exit strategy, but this may take a few years to achieve.

While ANDS was written with donor funds and developed under UNDP administration, some of the Afghan consultants involved still believe that it was not fully outsourced. They feel that they managed the project themselves, while the donors feel that they also played a part in managing this project with the help of the international agencies. The project sat outside the government structure until the document was completed. It is only recently that ANDS has formally become part of the government, within the ministries of finance and economy.

ANDS is seen as the roadmap for the country's development and its success is key for the future of this country. However, whether it will be a success is yet to be seen. UNDP will only hand it over fully to the government if all donors are happy and confident that there is capacity within the Afghan team to manage it without any external intervention.

### **Chief Financial Officer capacity building**

This project, to build the capacity of the newly-established Chief Financial Officer (CFO) positions in a number of ministries, took place in 2004. The project was funded by the WB and contracted to Maxwell Stamp. Eight ministries were identified as pilot projects and eight consultants were hired, one for each CFO. When the contracts were being prepared in early 2003, leadership was fairly weak in the Ministry of Finance's budget department (the co-signer of the project). Although an open bidding process was used, it turned out that the company ultimately chosen was not suitable for delivering the required services. The company did not even manage to get the team leader to start work on time. It took 10 months before the appointed team leader finished his assignment in another country and came to Afghanistan. Without the team leader, the other consultants could not start working. By the time the team leader joined, all the consultants who had applied were no longer available. The ministry brought in new consultants, but most of these had less experience than the original applicants. When the project began, the performance of the international staff was not good and they had insufficient experience of working in a fragile state like Afghanistan. In 2005 it was decided to terminate this failed project completely. Even though the government had to pay penalties for early termination, this decision was regarded as sound.

### **Justice sector reform**

This project is being managed by ASI, and is currently funded by the European Commission (EC). Other donors also have projects in this sector. While the lead donor is Italy, the EC contracted ASI to carry out various reform and legislative activities in the Ministry of Justice, the Supreme Court and the Attorney General's Office. In 2005 the government asked USAID to train the staff in this sector because the relevant ministries and directorates lacked the capacity to do so. USAID took on this contract as part of a bigger programme of judiciary system support which it had started in 2004. The contract was given to Checchi and Company Consulting Inc., who have trained the judicial system staff. USAID is happy that the project has been completed successfully. However, if you ask the Afghani people, they still complain about corrupt and incapable judges across the country (all judges were trained through this programme).

### **Private sector development**

The reform of the Ministry of Commerce and Industries (MoCI) was contracted to ASI to formulate the relevant policies. The three main work streams are investment policy, market business development and outreach. Since 2003, the MoCI has also contracted out a complete business registration service called the Afghanistan Investment Support Agency (AISA). This is a one-stop shop where investors can get information and register their companies. The result has been good: a process that used to take weeks now takes only days. Furthermore, AISA is now self-sufficient.

BearingPoint is also involved in MoCI and has taken responsibility for drafting nine laws since 2002. Some have already been passed, while some are still in parliament.

The Export Promotion Agency is another unit contracted out completely and run by a semi-independent unit. Its management reports to the ministry, while GTZ (the German official development agency) provides the funding. The agency is expected to be self-sustaining by 2011.

The Export Promotion Agency plans to work on revenue-generating programmes, but their full implementation is not possible at this stage. They hope that in the next couple of years they will manage to encourage more businessmen and women to pay for their services. Although GTZ is intending to stop funding this agency in the next two years, they are not certain the revenue generation plan will work in time for them to withdraw and fully handover the agency to the management team. GTZ has given the Afghan managers almost full autonomy, but under the watchful eyes of the German consultants working with them. Capacity building is an ongoing process in this agency.

Under new leadership, the ministry has worked closely with consultants to write a complete business plan, currently supported through DFID funds. The plan will help the ministry develop its five-year strategy, including the transition to self-sufficiency and a greater reliance on revenue-generating services. This project, begun in early 2009, has been contracted out to ASI to manage. ASI has recruited a team of international and national staff to complete the business plan and start on the next phase of ministry reform. The ministry has to remain a policy-making entity; it is not its job to implement projects for the private sector. Its responsibility is to facilitate the national and international private sector through sound laws and regulations and policies to help investment and growth of the country's private sector. However, the other offices that have been contracted out should start becoming self-sufficient.

### ***National Solidarity Programme***

The NSP, designed in 2002, is one of the most successful government programmes. It quickly caught the attention of the donor community, which has committed hundreds of millions of dollars every year to it. The programme makes money available for village clusters (a group of community councils) to prioritise and pursue their needs. A maximum of USD 60 000 per year can be transferred to each village to implement projects. Implementation is done by the community with the help of a facilitating partner, such as an NGO.

The NSP is the main government programme that shows the people that their government is doing something for them. The programme idea emerged under the direction of Dr Ashraf Ghani – then advisor to the UN Special Representative of the Secretary General. He called on his former colleague Scott Guggenheim, who was in Indonesia implementing the successful Kecamatan Development Programme. Guggenheim came to Afghanistan in January 2002, consulted with various national and international bodies, and established the concept of the NSP. Together they managed to convince the WB to pay for the initial costs and signed an agreement in May 2002. When the new Minister of Rural Rehabilitation and Development (MRRD) started working together with his team, they were given the NSP concept to design.

Initially, between 2003 to 2006, GTZ was given the management contract. After that, management reverted to the Ministry of Rural Rehabilitation and Development (MRRD), but the financial management has been outsourced to Maxwell Stamp. However, the ministry is apparently unhappy with how the company is handling financial management. The main problem involves slow procedures, which lead to unnecessary project delays. Another shortfall is that the evaluation and monitoring of the programme is done by ministry employees and donors. A third party has yet to critically monitor and evaluate this programme. The ministry plans to take over the financial management of NSP gradually in the next couple of years. This means that great national and in-house capacity will be required at MRRD to handle financial management.

At the design phase, a number of international consultants were contracted under the guidance of the deputy minister who still leads this programme (now as minister). As the ministry is

predominantly about making policies, it decided to contract international organisations to run this programme. The management of such a large programme was not easy, with projects operating in numerous provinces and with several facilitating partners.

The donor community has committed to contribute to this programme through the Afghanistan Reconstruction Trust Fund, but the financial management of a programme involving hundreds of millions of dollars every year needs financial management and accountability of a very high standard. Therefore, although the contracted company is not very successful, the donor community receives good and timely financial analysis and reports, as do the Afghan leaders such as the minister, deputy minister and the CEO of NSP within MRRD.

### ***The Counter Narcotics Trust Fund: a case study of failure***

This case study examines the failure of the Counter Narcotics Trust Fund (CNTF). The programme was to help financial manage a process to address the overwhelming challenges of narcotics in Afghanistan and pave the way for better programming and investment in counter-narcotic efforts. Narcotics still remain a great threat to the future of Afghanistan. They fuel terrorism and insurgencies that have dramatically affected the governance and state building processes. The failure to manage the fund allocated to such an important programme could be one of the main causes of the drugs problem around the world. We therefore feel that this case is a good example of a government and its international partners failing due to the bad management of an outsourced project.

As narcotics were a threat for the country and the region, the government of Afghanistan and the donor community sought ways to best implement counter-narcotics efforts and to use financial resources more efficiently. In October 2005, some donors proposed establishing a trust fund to be managed by the United Nations Development Program (UNDP). Another mechanism was discussed at the same time, which involved funding the counter-narcotics efforts via the government treasury. However, because of donor concerns over the lack of capacity and the incidence of corruption in the public sector, and taking into account the magnitude of the narcotics problem in Afghanistan and its potential “black” income, CNTF was set up to provide efficient and demand-driven financial management in a more transparent and accountable manner. It was to enable the government to address the lack of support for programmes and projects designed to replace poppy cultivation in the country.

The main objectives of the fund were the strategic priorities of the National Drugs Control Strategy (NDCS). In 2004 the Ministry of Counter Narcotics released a new strategy which set precise benchmarks for tackling narcotics through a programmatic approach. The fund was contracted out to the UNDP as a sole-source contract. A management board was established, including the government, UNDP and some donors such as the UK and the US. UNDP was tasked to administer the fund, but full responsibility for the nationally managed programmes remained with the Ministry of Counter Narcotics and Ministry of Finance.

In June 2007, UNDP reported that of the planned budget of USD 900 million, only USD 3.4 million had been spent (approximately 2.6%). This indicated a serious failure in counter-narcotics efforts and financial management. Most of the projects implemented and funded by CNTF are fragmented and operate in isolation from each other. The projects are small-scale (*e.g.* mushroom cultivation, greenhouse projects, honeybees, small-scale drought-related projects etc.) and the process lacks a strategic and programmatic approach. As the fund was poorly delivered and supported by donors, there has been little or no incentive for the line ministries to come up with new projects because their experience does not allow them to further invest in these projects. Instead, there have been other mechanisms in which they could invest for faster results. Lack of financial management capacity,

limited capacity in the lead ministry, limited support from the international community, and the lack of precise policy guidance for fund management are the key factors that undermined the overall performance of CNTF. A lack of consensus on counter-narcotics approach among key donors and the government of Afghanistan in 2006-2007 also dramatically undermined the performance of the fund and the country's counter-narcotics efforts. It also seems that the fund has not taken into account the institutional structure of the counter-narcotics entities in the country. The Ministry of Counter Narcotics (MoCN) did not exist in Afghanistan previously. In fact, there was no need for such a ministry. Instead there should have been a high-level directorate under the President. The main role of the MoCN is to formulate policies and co-ordinate the counter-narcotics efforts. Unfortunately, this has not been done efficiently. Too many players have been selected to implement the projects, and this has resulted in fragmented efforts. The fund mechanism failed to establish a programme framework to enable the implementing partners to work within a structure.

The fund required ministries to submit their project proposals to the CNTF management board, which reviewed and approved projects. The management board involves not only the government and UNDP, but also key donors. This could have been an advantage in managing the fund; more ideas around the table should have led to a more effective project. However, the presence of certain donors on the CNTF management board has challenged government ownership. Each donor has their own priorities and favourite projects, making decision taking difficult and overlooking the priorities of the Afghan people in the process. The CNTF management board differs from that of the Afghanistan Reconstruction Trust Fund (ARTF), which administers a total of USD 1 billion annually and whose executive boards members consist of the World Bank and the government – not donors. Furthermore, the CNTF has operated in isolation from the enabling environment, and has not addressed the capacity building of the Ministry of Counter Narcotics and other implementing ministries.

The key step in the procurement process (translating the approved projects into action) is still time-consuming. These quick-impact projects seem of low quality and are unrelated to each other. The capacity of the implementing ministries such as Agriculture, Rural Development and Public Works have been reportedly low because less attention was given to their CNTF-funded projects. The main reason has been that these projects were not priorities for those ministries. In the three years that the CNTF was implemented it underperformed and lost credibility. CNTF was bypassed; more direct approaches were sought to support the programmes and projects – especially in the agriculture sector. The mechanism didn't help to build the capacity of government institutions to run the fund. And this also resulted in the failure of proposed exit strategy. Its final failure was not building the trust of the donors to use the CNTF as a core mechanism for more co-ordinated interventions.

In the long run it is predicted that the fund should flow through the government's core budget; in other words the government of Afghanistan should take the lead in financial management of the counter narcotics efforts.

### **Health sector contracting-out**

This has been one of the most successful sectors, operating since 2003. This sector is mainly assisted by NGOs; the private sector has not shown much interest in government contracts due to their low profitability. The only way for the private sector to make money in the health sector is through private hospitals. Private businesses are licensed to do the job autonomously, rather than partnering with the government. The NGO sector partners with the government across the country. The donor community has been assisting the Ministry of Health with these contracts. The main donors are the WB, USAID and the EC. However, the EC has always been interested in running the show themselves. They have their own rules and regulations and do not work directly with the government. Their so-

called “external budget” is not part of the government budget, because they grant and monitor the contracts independently. Their package of health, however, is the same package that is designed by the ministry. The EC will start putting their funding into the core national budget sometime from 2010/11.

Of Afghanistan’s 34 provinces, the government has decided not to outsource clinics in three (Parwan, Kapisa and Panjsher). In these three provinces, the government has managed to provide all the basic health services through ministry-run hospitals and clinics. According to the Policy and Plan Director, there is not much difference in terms of service delivery and cost between outsourced and government-provided services. The government is able to provide almost all the services that an NGO would provide at the same cost and quality. Contracting-out as a whole, however, is cost-effective. Most of the city hospitals belong to the government and are run by the ministry. But in seven provinces, even the city hospitals are outsourced to NGOs with funding from the US, International Committee of the Red Cross (ICRC) and, in one case, by the EC. Evaluation reports by the Johns Hopkins University and IIHMR for 2006, 2007 and 2008 (The Afghanistan Health Sector Balanced Scorecard) show remarkable improvement in the services provided through NGOs. An advisor to the Minister of Health stated in an interview that the services provided by NGOs have improved in quality because of competition. He was, however, concerned about the low capacity of the ministry for monitoring and evaluation (M&E). Furthermore, he felt that the ministry should focus on building strong M&E so as to improve the quality of service still more.

### ***The Making Budgets and Aid Work project***

The Making Budgets and Aid Work project initially started as the Aid Co-ordination Project in 2003 with the support of UNDP and various donors. It is an ongoing project within the Ministry of Finance (MoF), and has over 75 staff. The then Minister of Finance was the visionary behind the reform. He saw financial management in a fragile situation as the key for any development or donor contribution. He later pointed to sound financial management as one of the 10 key functions of a legitimate state (Ghani and Lockhart, 2008). At the time, some processes in the MoF (such as budget) resembled a wish list. After the Bonn process in 2001, which established the first Afghan government following the fall of the Taliban regime, one of the main priorities for Afghanistan was to manage an accountable, reasonable and efficient financial system. This vision was later re-emphasised in 2004, when the Berlin donor conference was planned and presented to donors as part of Securing Afghanistan’s Future (multi stakeholder paper, March 2004). The vision for the budget process was defined as multi-year, comprehensive, results-based and supported by a strategic planning process.

In order to prepare such a sound operating and development budget, suitable capacity was needed. The existing staff of the ministry had no experience in designing the kind of budget the new leadership envisaged. The donor community was also concerned that without a systematic approach and a mechanism that could be monitored and evaluated, taxpayers’ contributions would be wasted.

The new leadership of the ministry wanted to lay the foundations of a system that could not be influenced by corruption; one that would facilitate accountability or force the managers to be accountable to the people and to the donor community; and one in which the donor community could invest. The General Director of Budget agreed with the UNDP that the ministry would raise the funds from the donor community and the UNDP office would administer a team to set up and start work on the development budget. While civil servants had the capacity to run the ministry’s operating budget (covering day-to-day expenses of the government entities), with new pledges coming in for reconstructing the country, a new mechanism was needed to manage the funds and allocate the development projects.

At the time, an independent team responsible for aid co-ordination and seconded by UNDP had just finished its first phase of activities, but the government had not decided where to reassign them. The Director of Budget asked UNDP to second this team to the Ministry of Finance in order to set up and run the development budget department until the capacity of the civil servants was built and the ministry itself could take over the function. UNDP agreed and a contract was signed between UNDP and MoF with funding that was, at the time, available through UNDP under the name of the Aid Co-ordination Unit.

This team consisted of one international consultant and eight national consultants with knowledge and experience in aid co-ordination and data analysis. Later, when the initial funds were running out, other donors became interested and contributed to this project through UNDP. For example, in 2003, the US Embassy and USAID showed an interest when the Ministry of Finance needed further funding for the development budget team. The unit then expanded to three international and several national consultants, who designed the first national budget in 2003. The main long-term donors have been CIDA, the US, UNDP, Italy, the Netherlands, and GTZ.

The 2001 Bonn Agreement increased the number of ministries; new staff inherited from other ministries had no experience of budget preparation. A group of advisors to the MoF and the WB commented that the job of the budget team in the Ministry of Finance was especially critical for preparing the ministries' budgets and carrying out some capacity-building workshops and courses (Carnahan *et al.*, 2004). The budget preparation in the early years was a challenge that the government could not have performed well without the support of contracted out projects. The commitment of donors was crucial in this period, as was the administration that UNDP provided, despite some problems. With such low capacity in the treasury system and the increasing corruption in the country, the donors would only trust an external and independent entity such as UNDP to administer the money they had provided to support the country.

Donors and the UNDP understood the need for the government to own the project and worked alongside the leadership of the Ministry of Finance. However, the capacity and capability of the UNDP international staff themselves were questionable, as they had little experience or understanding of a post-conflict country and a fragile government. The bureaucracy of the UN system was another challenge with which the MoF leadership had to deal. The alternative however, would have been the United Nations Office for Project Services (UNOPS), which was famous at the time for its low capacity, inflated charges and high corruption. The leadership did consider contracting out to the private sector, but costs would have been higher than with UNDP. UNDP started with 3% charges (later increased to 6%) to run and manage the project; a private company would have charged many times more.

Following the success of the budget preparation phase, the execution phase also needed to be reformed. BearingPoint was contracted by the government using USAID funding to oversee the reform of the Treasury Department. A computerised system of cheque issuance started operating in Kabul so it could report immediately on expenditures. Other provinces also increasingly started to computerise their systems. Accounting system reform in Treasury, however, was funded by the WB and implemented by BearingPoint, while other areas in Treasury were funded by USAID. The entire contracting out process lasted from 2002 to 2008. Some of the projects have now been completed and handed over to the ministry to manage. However, some international consultants do remain to assist the ministry staff and work on further capacity building. Also some functions are still managed by the international organisations, but on a smaller scale.

A 2007 UNDP evaluation of the Making Budgets Work project stated that it had made significant improvements and had achieved much in terms of its goals (UNDP, 2007). This evaluation recommended that further funds be raised for the project to continue and to expand to play a key role

in the improved development of the Afghan government and, therefore, of the country. By hiring a small number of international consultants, but a larger number of Afghan consultants working in the MoF, the project has managed not only to improve the performance in the Ministry of Finance, but also to assist other ministries in building their capacity. Most of the Afghan managers have been through many training programmes and capacity development projects and are ready to manage without much help from international consultants. MoF staff have constantly been in touch with the budget teams in the ministries and held training programmes. In most of the ministries there are also international advisors assisting in capacity development. Their own initial instructions however, mainly come from the MoF budget team.

This project has also minimised corruption by creating a transparent budget. Some initial steps have also been taken to begin provincial planning and programming. Provincial planning may be only a first step in this direction, but it is certainly a significant start in Afghanistan.

The aid co-ordination part of the Making Budgets Work project has also played a significant role and has been fairly successful. Donors have been co-operative in providing relevant information. As a result, they have benefited from information analysis to help them make crucial decisions, to avoid duplicating efforts, to be aware of each other's activities, to feel accountable and to ensure that all information is transparent. The increased contribution by donors to the government budget, such as the use of the Afghanistan Reconstruction Trust Fund (ARTF) rather than donors funding projects externally, is one of the most positive results. Yet, a portion of donor budgets still goes directly to their implementing partners; such funding may need to continue because it is particularly useful for emergency and quick-impact projects. Furthermore, the ARTF process is time-consuming and cannot cover for all projects.

The ministry also contracted out the costing of the Afghanistan National Development Strategy (ANDS) to Maxwell Stamp with funding from DFID towards the end of 2007. However, this was later handed over to ASI. This function will now move to UNDP as part of the overall Budget Department support. Two national and one international consultant completed the first phase of the ANDS costing. The second phase with ASI is about to finish as the final report is being prepared and will then be handed over to UNDP. The Ministry of Finance, despite improved capacity, still relies on these international and national consultants rather than on its own civil servants. Only these highly paid consultants can perform procedures that are very new in Afghanistan. And since most of the projects are designed to deliver results quickly, it becomes difficult to add a capacity-building component to them. Some capacity building is always included in the memoranda of understanding (MoUs) and in the contracts, but in reality the Ministry of Finance does not have the resources to effectively train a good civil servant workforce. As stated in the evaluation of the Making Budgets Work project (UNDP, 2007), the ministry may need the help of consultants for a longer period of time. It is therefore suggested that a group of national consultants be trained to take over the functions to reduce reliance on international consultants with their high hardship and security costs.

## **Lessons learned in Afghanistan**

Various lessons have been learned through the many years of contracting out experiences in this country. Putting these lessons into practice, however, remains vague and largely ignored by the national and international community involved. The following overall lessons should be learned:

1. The government needs to assess needs more comprehensively before contracting out a function. The impacts should also be evaluated and possible side-effects explored at the beginning of the process. Decisions have been made hastily while trying to meet the

expectations of the local public as well as the international community, all of whom want quick results. These quick decisions were made by a fragile state which was expected to start functioning quickly.

2. A systematic approach and the long-term identification of expected results are important in contracting out. Piecemeal approaches have been offered at times to address problems, and small-scale capacity building projects have been designed to address immediate needs, rather than trying to build long-term institutional capacity.
3. Ownership and capacity building are correlated: while there has been emphasis on government ownership, there should have been parallel capacity development of government institutions. The government still lacks capacity in many sectors and a large capacity development programme is yet to be designed.
4. Government ownership of a project is essential, but mutual accountability based on a transparent system is also a must. This is useful when civil society is weak and the international community is a source of funds. The level of corruption is very high in Afghanistan because donors do not follow up on the funds they provide and do not ask for the punishment of corrupt entities.
5. Government leadership is essential in the decision-making process when an outside organisation is running the function. If the government leader is asking for assistance in the decision-making process, the international or outside partner can give advice. But the priority should be given to the original stakeholders of the project. In most cases consultants have made decisions without confirming with the government manager or counterpart. In weak states, consultants should ensure the government partner knows the implications of the decisions being made.
6. A balance between service delivery and long-term capacity building is necessary. Sometimes it is easier to deliver the service on an *ad hoc* basis rather than to invest time in capacity-building. Capacity development projects should at times be separate to the one that is providing a service. In some projects this has been planned, but others had no capacity building component or any type of planned exit strategy.
7. Experiences in Afghanistan show that the more functions are contracted out, the longer it takes to build the capacity of civil servants. This is probably a sacrifice the Afghan people should have been made aware of. There were no such studies when the new government took over and decided to start reforming processes with the help of international capacity. The international consultants and technical advisors that came into the country focused more on doing the job and had no time to worry about building the capacity of their local counterparts.
9. One of the key components of any contracting-out project should be to consider macro policy which guides the project and programme formulation.
9. The donor community should consider the country's policies and priorities, rather than its own political agendas. One example is "tied aid", where the donor must recruit a company from their home country to deliver the service, even though this company may not have the relevant experience, know-how or knowledge of the cultural background of Afghanistan. But "one size doesn't fit all"; in the case of consultancy companies, a successful consultant in one country doesn't guarantee success in another. While a

company may have been successful in a European country like Kosovo, the context is quite different to Afghanistan.

10. Co-ordination among donors and service providers in an office is important if the work is contracted out to different organisations serving the same department/ministry. However, not many managers have the time or capacity to prioritise this task. Bureaucracy takes up much of the managers' time, leaving little left to ensure the smooth co-ordination of the various donors. As a result there has been some unhealthy competition amongst the various international bodies involved.
11. Some donors can be overambitious and want to be seen in many different government offices and sectors showing assistance and help. This has sometimes meant they failed to manage even one project well. Donors should choose only one or two sectors and concentrate on supporting them either through private sector contractors or NGOs, rather than picking a lot of functions and sectors and then not being able to find good companies and consultants to perform and deliver good results.
12. It would be preferable to have no more than two service providers involved in one project. In the justice sector there are currently six (The United Nations Assistance Mission in Afghanistan projects and advisors, UNDP, DFID, US, Italy, the WB, etc.). There is not enough internal co-ordination, and their priorities also differ from those of the Afghan government. This sector therefore does not have much capacity.
13. With a national development strategy only becoming ready in 2008, many areas have lacked sound policy guidance, which has affected implementation and undermined the process credibility. ANDS will hopefully fill that gap, but it first has to be translated into practical policies.
14. The UN ought to play a more influential and co-ordinating role, and should bring all donors around one table to avoid duplication of effort since most of the contracting-out decisions are made directly by the donors. The government alone does not make such decisions and the international community is always involved in the process. The government does not usually have the ability to co-ordinate donors. Even if the government wants to co-ordinate them, the donors do not co-operate; in this case UNAMA would be a better choice.

## Key recommendations

The following recommendations could apply to many different regions in the world and many different contexts. Nevertheless, each country will have its own priority needs; identifying those needs is a first step to any contracting out decision:

- ▶ A programmatic approach is recommended rather than a small project-based approach, to ensure that the government's main priorities and programmes are met.
- ▶ An exit strategy is necessary when a function is being contracted out. This must be prepared early enough to plan for the future capacity building of the local workforce.
- ▶ Including a capacity development plan in the contracting-out process is very important; it should focus on local civil servants.
- ▶ Ownership is paramount to ensure that the government understands and adopts the process.

- ▶ There should be a mutual accountability mechanism in place to assure that the government, donors and implementing partners respond to the challenges.
- ▶ Sound monitoring and evaluation are necessary, both by donors and the government, to ensure that the service provider has delivered good results and laid a concrete foundation for the function.
- ▶ When selecting consultants, priority should be given to regional experience or individuals who have already worked in other fragile states or on similar successful projects/contexts. South-South co-operation and contracting should be considered.
- ▶ Sole sourcing should be avoided as much as possible in favour of a more competitive approach.

#### **Box 4.1: Questions to ask when assessing contracts**

An official checklist for assessing contracts should be defined and implemented along the following lines:

- ▶ What is the need?
- ▶ What are the government's current capabilities? How much work can it do on its own?
- ▶ Will the need be fulfilled by contracting out this function?
- ▶ How do the current political and economic conditions affect the circumstances?
- ▶ What is the objective of the contract? What is the expected outcome?
- ▶ What are the candidate partner's credentials?
- ▶ How much experience does the candidate contractor have in this work?
- ▶ Who are its referees?
- ▶ What is the educational background of its staff?
- ▶ Does the candidate have any political motives? Is it influenced by another government?
- ▶ Does the candidate speak our language? What is the cultural fit?
- ▶ What are the concrete deliverables? By when?
- ▶ What are the risks of contracting out to them? What is the worst-case scenario? Can we accept this risk?
- ▶ Does the contractor have any conformity obligations (technical, cultural, practical)?
- ▶ What does the partner guarantee? Who are the guarantors/backers?
- ▶ How much local (Afghan) content should we demand?
- ▶ What does the local staff-development programme look like?
- ▶ What criteria should we use as performance indicators?
- ▶ Who finances the project? Who controls the budget?
- ▶ Who has authority to say "No" after the work starts?
- ▶ Are there penalty clauses in case the partner does not perform?
- ▶ How long does the contract last?
- ▶ What are the contract termination conditions?
- ▶ Whose law applies?

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## **Endnotes**

72 Also, USAID's tied aid policy doesn't allow projects to be given to non-US companies; this policy is often criticised.

## **Annex 4.A1. Interviews**

Dr Mustafa Mastoor, Deputy Minister of Finance

Ian Holland, Deputy Director of UNDP

Dr Abdula Fahim, Senior Advisor to the Minister of Public Health

Dr Ahmad Jan, Director of Policy and Planning of Ministry of Public Health

Halim Wahedi, Director of Counter-Narcotics Trust Fund

Richard Bontjer, Former Advisor to the Ministry of Counter Narcotics

Shafic Gawhari, Country Director (IS), GTZ, Kabul

Wahid Waissi, Director of ANDS Coordination, Ministry of Finance

Wais Barmak, Deputy Minister of Rural & Rehabilitation and Development (former NSP director)

Zlatco Hurtic, Advisor to Aid Coordination Unit, Budget Team, Ministry of Finance



**From:**

## **Contracting Out Government Functions and Services**

### **Emerging Lessons from Post-Conflict and Fragile Situations**

**Access the complete publication at:**

<https://doi.org/10.1787/9789264066212-en>

#### **Please cite this chapter as:**

Ghani, Seema and Nematullah Bizhan (2009), "Contracting out Core Government Functions and Services in Afghanistan", in OECD/African Development Bank, *Contracting Out Government Functions and Services: Emerging Lessons from Post-Conflict and Fragile Situations*, OECD Publishing, Paris.

DOI: <https://doi.org/10.1787/9789264066212-5-en>

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