Financial Governance Report

Financial Governance Committee

May 2018

THE WORLD BANK

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01 About the Financial Governance Committee

The Financial Governance Committee (FGC) was established in early 2014 by mutual agreement between the Federal Government of Somalia (FGS), donors and International Financial Institutions (IFIs) to provide a forum for dialogue and advice on strategic financial governance issues. Members of the FGC are drawn from Somali institutions and international partners. The FGC is chaired by the Minister of Finance. Other FGS members include the Governor of the Central Bank of Somalia (CBS), the Minister of Fisheries and Marine Resources in his capacity as Secretariat of the Economic Committee of the Council of Ministers, representatives from the President's Office and the Prime Minister's Office, the Chair of the Parliamentary Finance Committee and the State Attorney General. The FGC has four international members, who sit as delegates on behalf of the International Monetary Fund (IMF), the World Bank[1], the African Development Bank (AfDB)[2] and donor partners[3].

The FGC was established following the resignation of the Governor of the Central Bank of Somalia, Yusur Abrar, in late 2013, amid concerns over Government's management of recovered assets and the nature of a contract FGS had entered into with a US law firm to assist the asset recovery process. The FGC's initial focus was on Central Bank Governance, asset recovery and public procurement and concessions. In response to emerging demand, the FGC has subsequently started monitoring FGS progress in implementing public financial management (PFM) reforms in the context of the IMF Staff Monitored Program (SMP). It has also provided advice on specific financial governance issues that impact on overall governance such as security sector expenditures, natural resource revenue management, public property protection and fiscal federalism.

Until such a time as the Procurement Act is under full implementation, the FGC has been mandated by the FGS to review and provide advice on all Government contracts and concessions above $5m in value[4]. It also supports the work of the Interim National Procurement Board (INPB), an FGS committee mandated to approve all concessions and contracts above $2m. The FGC's current mandate runs to the end of June 2018. Its renewal will be subject to discussion between the incoming Government and the international community.

1 Funded through the World Bank Multi Partner Fund. The fund has ten contributing donors – for further details see: http://somaliampf.org/development-partners

2 The FGC is awaiting the appointment of a new AfDB delegate

3 Funded on behalf of donors by the European Union

4 See Annex 1 for a list of all FGS contracts reviewed by the FGC since 2014

04 Executive Summary

Good financial governance is essential to Somalia's State-building process. Somalia currently faces the following primary State-building challenges:

1. Combating insecurity
2. Developing a viable system of federal government
3. Attaining fiscal sustainability
4. Fostering inclusive growth and generating employment
5. Delivering essential services to citizens
6. Enabling investment in longer-term recovery and development

Corruption enabled by poor financial governance can fatally undermine the State's ability to address its State-building challenges. State corruption, perceived or actual, reinforces perceptions of inequality and State bias, reduces the State's capacity to deliver its core functions and negatively affects the willingness of third parties to co-operate with the State. Conversely, sound financial governance is expected to help reinforce the legitimacy of the State, enable the development of a viable federal system of government, promote stability, open the door to debt relief and enable access to the financial flows essential to rebuilding the country.

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The 2017 FGR identified seven strategic challenges the Federal Government of Somalia (FGS) needs to address if it is to strengthen financial governance:

1 Agreeing a coherent way forward on fiscal federalism

2 Managing natural resources transparently and equitably

3 Raising domestic revenues

4 Strengthening the credibility of public procurement and concessions

5 Strengthening expenditure management

6 Developing the financial sector

7 Increasing access to external financing

The transition in Federal Government administration in March 2017 created an initial pause in financial governance reforms, as new players familiarised themselves with the issues and determined their priorities. The new administration is to be commended for its strong commitment to implement policies and reforms under the IMF Staff-Monitored programme (SMP), which it took over from the previous administration, and the progress it has made in meeting its targets.

The transition in administration created opportunities to revisit several financial governance challenges through a new lens. The new administration took an early decision to review all existing Government contracts, with a view to renegotiating or cancelling them as appropriate. It also reinvigorated the dialogue between the Federal Government and FMS on fiscal federalism. Likewise, the political legitimacy endowed on the new administration by the transition enabled it to create momentum behind the FGS's legislative agenda and to reach out to taxpayers.

Tangible achievements over the past year include: passage of the National Communications Law, paving the way for sector regulation and revenue collection from the telecoms activities; agreement between the Federal Government and Federal Member States on an interim process for fisheries licensing; agreement to levy a common tariff on specific goods at Federal and Member State level; review and subsequent cancellation of several concessions to private sector companies for collection of non-tax revenues following a determination that they failed to deliver value for money; expansion of the federal tax base into new areas such as sales tax; and, biometric registration of around 5,000 Somali National Army (SNA) personnel as a precursor to paying their salaries direct to bank.

Some financial governance issues lost momentum in the transition. Relatively little progress was made with respect to the development of public procurement capacity and establishment of conditions for effective implementation of the 2016 Procurement Act. There was a hiatus in the implementation of interim procurement measures to guide public procurement until such a time as the Procurement Act is fully effective. It also took a while for the protection of public property to gain executive attention and there remains much to do to keep this issue alive.

Progress towards stronger financial governance is not always linear. The irregular cancellation and re-award by the SNA commander of the SNA rations contract in April 2017 was a significant setback at the outset of the new administration's tenure. The Ministry of Finance subsequently conducted a legal review which determined that the cancellation and re-award was irregular, and the Economic Committee of the Council of Ministers resolved that the contract should be retendered. However, the decision has not yet been implemented. One of the major financial governance tests of 2018 will be the extent to which the Federal Government can bring greater order and transparency to security sector expenditures.

More broadly, in spite of high-level political commitment to strengthening Government contracts and the passing of the 2016 Procurement Act, procurement capacity and understanding of procurement due process remains limited across Government. In general, putting in place new legal frameworks and establishing appropriate policies only constitute initial steps towards stronger financial governance. Effective implementation is needed for these frameworks and policies to achieve their intended objective.

Although the level of dialogue between Federal Government and Federal Member States on fiscal federalism is encouraging, the current political momentum towards reaching a comprehensive agreement on revenue sharing between FGS and FMS needs sound technical underpinning. High-level revenue sharing principles should be agreed before percentage shares are determined.

The FGC's top ten priorities for 2018 focus on short term actions that will enable the Federal Government to support its state building agenda and demonstrate its continued commitment to reducing the scope for mismanagement of public resources. Their effective implementation will be contingent on political commitment at the highest level; increased Federal Government capacity to work effectively with the Federal Member States on an agreed financial governance agenda; increasing co-ordination between individual federal agencies; a continued culture shift away from legacy practices such as sole-source contracting; and, outreach to the business community. Financial governance issues should also have a special place for discussion in the ongoing constitutional discussions focusing on fiscal federalism and resource sharing.

Top ten Financial Governance priorities in the coming year

1. Complete registration and payment to bank of all security sector personnel, including cash for fresh rations ('idaan')
2. Re-tender SNA and Prisons rations contracts in line with interim procurement requirements and establish a strengthened rations delivery verification mechanism
3. Re-negotiate Port (Al Bayrak) and Airport (Favori) concessions, and resolve other outstanding legacy contracts from the previous administration (Sahel Airport Shuttle, Simatech Dry Port, Passports, Visas)
4. Ensure all new procurements of contracts and concessions are conducted in accordance with the interim procurement requirements
5. Reach an agreement between FGS and Federal Member States on the principles underpinning revenue sharing
6. Modernise the legislative and administrative framework for inland revenue in consultation with Federal Member States and business community
7. Agree a Customs Modernisation Plan with the Federal Member States which includes a roadmap for from transitioning from volume-based to value-based customs tariffs
8. Institute basic reporting on transfer utilisation and agree an objective basis for 2019 transfer allocations to Federal Member States and Banadir
9. Compile a full inventory of Federal Government property and begin to review all public property leasing and disposals since 2012
10. Implement the first phase of currency reform

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09 Abbreviations and Acronyms

AfDB	African Development Bank
ALSF	Africa Legal Support Facility
AML/CFT	Anti-Money Laundering and Combatting the Financing of Terrorism
BRA	Banadir Regional Administration
CBS	Central Bank of Somalia
EU	European Union
FGC	Financial Governance Committee
FGR	Financial Governance Report
FGS	Federal Government of Somalia
FMS	Federal Member States
GDP	Gross Domestic Product
HIPC	Heavily Indebted Poor Countries
HRP	Humanitarian Response Plan
ICAO	International Civil Aviation Organization
ICT	Information and Communications Technology
IFI	International Financial Institutions
IMF	International Monetary Fund
INPB	Interim National Procurement Board
LMTO	Large and Medium Tax Payers' Office
MAF	Mutual Accountability Framework
MoF	Ministry of Finance

MTB	Money Transfer Business
NDP	National Development Plan
NISA	National Intelligence and Security Agency
NSRC	Non-Salary Recurrent Costs
PFM	Public Financial Management
PRSP	Poverty Reduction Strategy Paper
PSA	Production Sharing Agreement
RCRF	Recurrent Cost Reform Financing
SFMIS	Somalia Financial Management Information System
SMP	Staff Monitored Program
SNA	Somali National Army
StAR	Stolen Asset Recovery Initiative
ToR	Terms of Reference
TSA	Treasury Single Account
UCS	Use of Country Systems
UCT	Upper Credit Tranche
UK	United Kingdom
UN	United Nations
UN SOMA	United Nations Status of Mission Agreement
US	United States
WB	World Bank

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Introduction

In March 2017, the FGC published its first comprehensive Financial Governance Report (FGR). The 2017 FGR provided an assessment of financial governance challenges in Somalia and recommended several priority actions to strengthen financial governance and state-building efforts in the next twelve months[5].

This second Financial Governance Report reviews the financial governance challenges currently facing Somalia. It then assesses the progress made in strengthening financial governance over the past year and explains the advice and support that the FGC has provided. It concludes by identifying ten priority actions for strengthening financial governance in the coming year.

UN PHOTO/STUART PRICE

5 See Annex 2 for a detailed description of progress in implementing the 2017 recommendations

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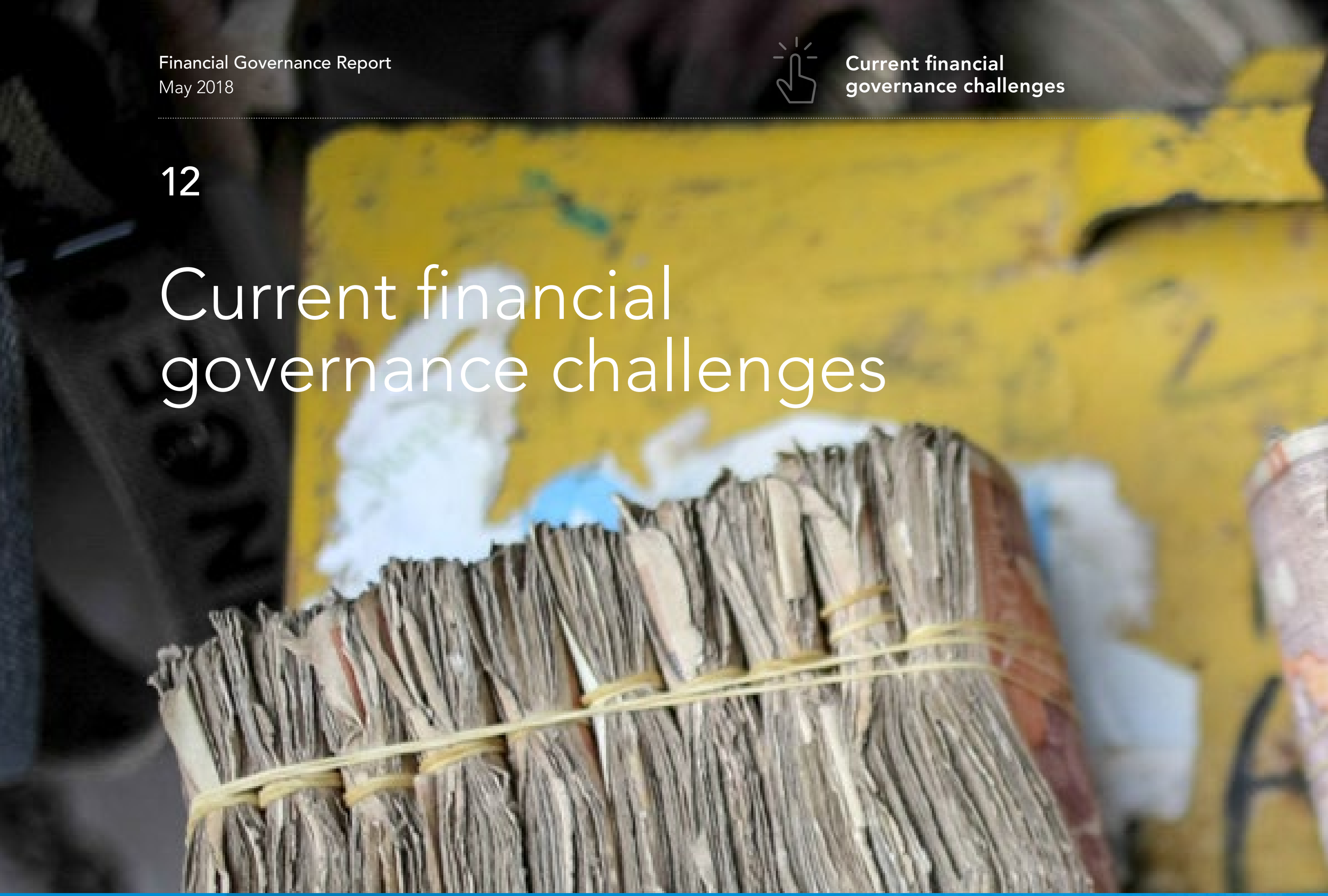
Current financial governance challenges



AU-UN IST PHOTO / STUART PRICE

Good financial governance is essential to Somalia's State-building process. Somalia currently faces the following primary State-building challenges:

1. Combating insecurity
2. Developing a viable system of federal government
3. Attaining fiscal sustainability
4. Fostering inclusive growth and generating employment
5. Delivering essential services to citizens
6. Enabling investment in longer-term recovery and development

Corruption enabled by poor financial governance can fatally undermine the State's ability to address these challenges. State corruption, perceived or actual, reinforces perceptions of inequality and State bias. The misuse of public resources (cash, natural resources and fixed assets such as land) and public goods (commodities or services that are provided without profit for the ultimate benefit of citizens) can be expected to negatively impact on:

- Public willingness to accept the authority of the State and pay taxes
- The ability of the State to provide core functions such as security
- The degree of co-operation of regional administrations in a federal system of government
- The willingness of the international community to provide aid direct to the State and as well as other means of financing such as debt relief
- The chances of attracting high-quality private sector investment to enable economic development and job creation

Corruption ultimately undermines the public's trust in its government and can become a conflict driver.

Conversely, it is anticipated that sound financial governance will help reinforce the legitimacy of the government, enable the development of a viable federal system of government, promote stability in Somalia, open the door to debt relief and enable access to the financial flows essential to rebuilding the country.

The 2017 FGR identified seven strategic challenges that the Federal Government needs to address if it is to strengthen financial governance. These challenges remain relevant in 2018.

Challenge 1:

Agreeing a coherent way forward on fiscal federalism

Fiscal federalism is the mechanism by which public sector functions and resources are allocated among different tiers of government through agreement on revenue authority, expenditure responsibility and mechanisms for resource equalisation. Current inter-governmental fiscal arrangements, including tax regimes, are not sufficiently harmonised. They have evolved by default and give a significant advantage to Federal Member States (FMS) that have access to port revenues and coastline. This runs counter to the principle of fair distribution of resources established in the Provisional Constitution and raises the risk of fragmented and uneven development across Somalia that undermines state-building. This risk, which at its most extreme tends towards 'economic balkanisation', is exacerbated by current tendencies of FMS to negotiate major concessions and infrastructure contracts unilaterally, without co-ordination with one another or FGS.

Challenge 2:

Managing natural resources transparently and equitably

Somalia has significant natural resource potential across a wide range of sectors. Access to natural resources revenues could potentially have a transformational impact on the state's finances and prospects for economic development. However, unless managed transparently, equitably and sustainably, natural resource revenues also carry a substantial degree of risk. They have the potential to generate conflict between communities and their governments, and between levels of government within the federal system. Depending on how they are spent, they also have the potential to undermine fiscal sustainability, disrupt economic management, foster corruption and generate inflation.

Fishermen: AU-UN IST PHOTO / STUART PRICE

Challenge 3:

Raising domestic revenues

FGS faces a severe resource constraint that limits its ability to support fiscal federalism and deliver core State functions effectively. The tax base is narrow, tax rates are low, and the tax collection system has been predominantly informal for many years. Nonetheless, taxpayers need to be convinced that paying more taxes to the State is in their interests, and that revenues will not be misappropriated. Raising revenues therefore requires a complex set of inter-linked actions; political commitment to tax compliance, dialogue with key taxpayers in key sectors, development of appropriate legislation, and greater technical capacity for collection and compliance. Government concessions to private sector entities to manage or support the collection of non-tax revenues also need to be transparent and offer value for money.

Challenge 4:

Strengthening the credibility of public procurement and concessions

Historically, the award of Government contracts has not been subject to open competition, fueling suspicions of corruption and bias in the selection of suppliers. There has been a similar lack of transparency around the disposal of public assets. The FGC has played a lead role in reviewing high-value FGS contracts and concessions since 2014. Most of the contracts reviewed by the FGC resulted from direct negotiations between FGS agencies and contractors, often instigated by the contractors themselves. Their terms rarely offered value for money to Government. Current FGS commitment to more transparent and competitive contracting needs to be sustained and deepened going forward if the Government is to strengthen the credibility of public procurement and concessions and improve value for money in the delivery of goods and services.

Challenge 5:

Strengthening expenditure management

Government expenditures have historically been paid entirely in cash. While this cash-based approach has been a function of the weakness of the payment and banking systems, it lacks transparency and creates ample scope for diversion of funds. As the capacity of the payment and banking systems evolve, the management of FGS expenditures needs to improve accordingly. FGS has embarked on reforms to the payment of salaries (direct to individuals' accounts) and non-wage expenditures (direct to suppliers) to reduce cash handling. These reforms need to be completed, particularly in the security sector. Advances to Government agencies also need to be fully accounted for before new ones are made. FGS also needs to strengthen its mechanisms for verifying the delivery of goods and services; particularly high-value rations contracts. The gains made in improving the transparency of public tendering will count for little if there is limited visibility on whether goods and services are subsequently delivered.

Challenge 6:

Developing the financial sector

Reforms to the regulation and supervision of Somalia's financial system are already underway. Reform areas include regulation and supervision of Commercial Banks, Money Transfer Business and Mobile Money Services, as well as Anti-Money Laundering and Countering Financing of Terrorism (AML/CFT) compliance. It is critical that reforms in these areas continue to be supported, politically, financially and technically. They will enable the re-establishment of correspondent banking relationships with international banks, thus safeguarding the flow of remittances into Somalia. They will also improve the FGS's prospects for accessing external financing and will support economic development by enabling the private sector to access credit through the banking system, rather than relying on informal credit networks.

Challenge 7:

Increasing access to external financing

Given its fiscal constraints, FGS needs increased access to external financing in order to consolidate the process of state-building and extend the development agenda. Good financial governance is essential to persuading creditors and donors of the value of extending additional financing to FGS. In the absence of additional financing, early stabilization gains are likely to be jeopardized. Achieving debt relief will be one way of unlocking additional external financing, as FGS will be able to access concessional loans from multilateral and bilateral lenders. FGS also needs to increase its access to grant financing.

Progress over the past year

Overall Assessment

The transition in Federal Government administration in March 2017 created an initial pause in financial governance reforms, as new players familiarised themselves with the issues and determined their priorities. The new administration is to be commended for its strong commitment to implement policies and reforms under the IMF Staff-Monitored programme (SMP), which it took over from the previous administration. It has made solid progress to date in achieving the targets set under the second 12-month SMP (May 2017 – April 2018)[6], including its targets for domestic revenue mobilisation. The third 12-month SMP (May 2018—April 2019) will continue to lay the foundation for Somalia to reach an Upper Credit Tranche (UCT) arrangement with the IMF, which will eventually pave the way for receiving debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative.

The transition in administration created opportunities to revisit several financial governance challenges through a new lens. The new administration took an early decision to review all existing Government contracts, with a view to renegotiating or cancelling them as appropriate. It also reinvigorated the

6 http://www.imf.org/en/Publications/CR/Issues/2018/02/26/Somalia-2017-Article-IV-Consultation-and-First-Review-Under-the-Staff-Monitored-Program-45662

AMISOM Photo

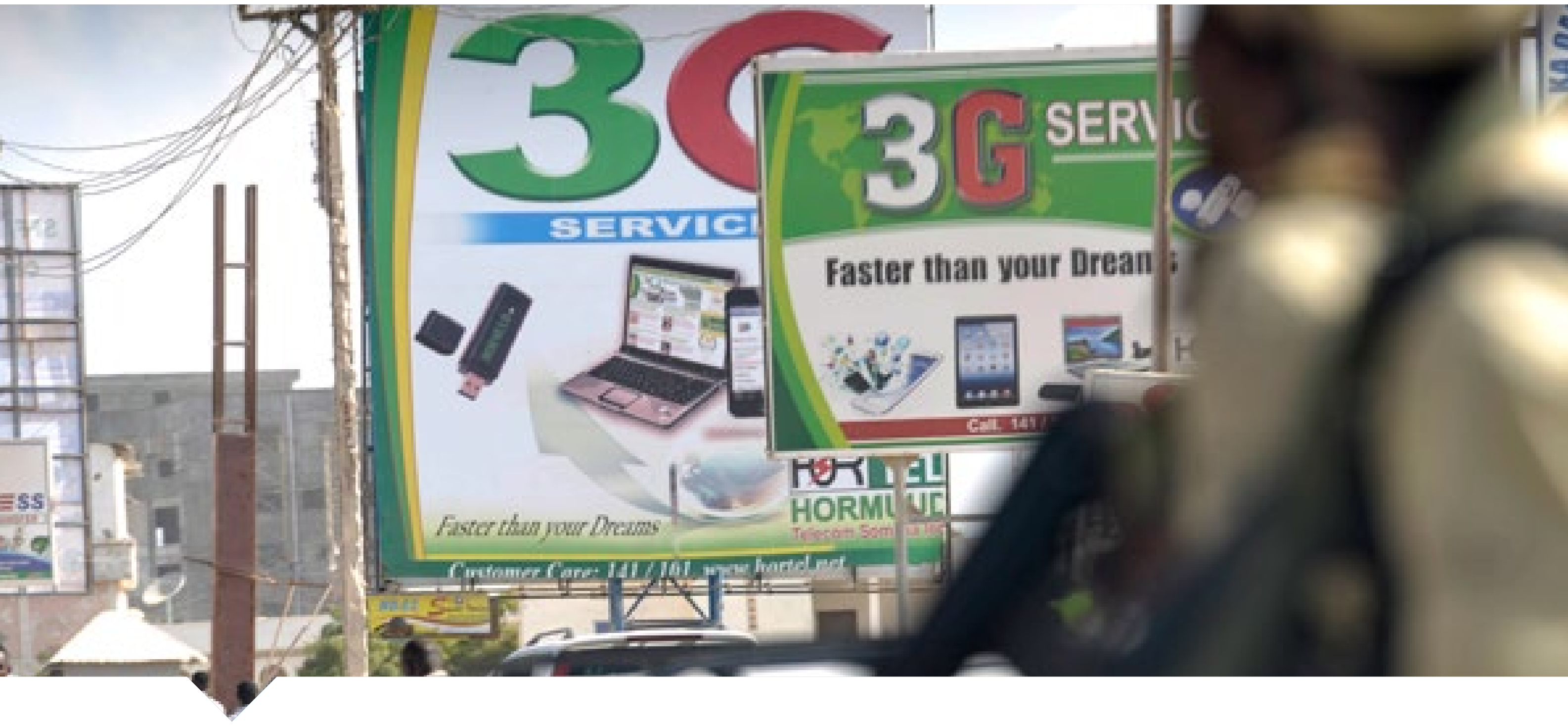
dialogue between the Federal Government and FMS on fiscal federalism. Likewise, the political legitimacy endowed on the new administration by the transition enabled it to create momentum behind the FGS's legislative agenda and to reach out to taxpayers.

Against this backdrop, the new administration has been able to register a number of tangible achievements. The passing of the National Communications (Telecoms) Law early in the administration's tenure reflected a successful co-ordinated outreach to the legislature and the telecoms sector and paved the way for sector regulation and collection of new revenues from telecoms. The executive has demonstrated strong political commitment to achieving fiscal federalism goals, including harmonising taxes and sharing resources equitably. An interim agreement has been reached between the FGS and FMS on fisheries licensing, and the Federal Minister of Finance and his FMS counterparts have agreed to levy common tax rates on specific items[7]. A number of concessions to private sector companies for collection of non-tax revenues[8] have been cancelled following a determination that they failed to deliver value for money; in spite of resistance from the companies involved, the services have now reverted to Government with revenue benefits. Efforts to extend the tax base into new areas such as sales tax on imports met strong initial resistance from the business community and from Parliament, but now appear to be yielding fruit. Efforts to register security sector personnel and pay their salaries direct to their accounts are ongoing, with around 5,000 SNA personnel already biometrically registered, although there is some way to go before they are successfully completed.

Some financial governance issues lost momentum in the transition. Relatively little progress has been made with respect to the development of public procurement capacity and establishment of conditions for effective implementation of the 2016 Procurement Act. Likewise, the transition created a significant hiatus in the implementation of interim procurement measures, intended to guide public procurement until such a time as the Procurement Act is fully effective, including convening of the Interim National Procurement Board (INPB). It also took a while for emerging issues such as the protection of public property to gain executive attention and there remains much to do to keep this issue alive.

In general, most progress has been made on issues where the Ministry of Finance and the Economic Committee of the Council of Ministers are recognised as having authority to be the lead actors and decision-makers. Progress has been slower on issues that require co-ordination with other stakeholders both inside and outside of Government. The ability to co-ordinate and develop consensus across stakeholders is a key element in tackling some of the most sensitive and important financial

7 Khat, cigarettes and departure tax
8 Road tax, property transfer tax, vehicle licensing



governance issues. Reforming security sector expenditures, natural resource revenue management, contract renegotiation, procurement reform, protection of public property all require concerted dialogue, openness and joint working with multiple stakeholders.

Progress towards stronger financial governance is not always linear. The irregular cancellation and re-award by the SNA commander of the SNA rations contract in April 2017 was a significant setback at the outset of the new administration's tenure. The Ministry of Finance subsequently conducted a legal review which determined that the cancellation and re-award was irregular, and the Economic Committee of the Council of Ministers resolved that the contract should be retendered. However, the decision has not yet been implemented, demonstrating the challenges inherent in acting on issues that require co-ordination across FGS agencies (in this case, the Ministry of Defence and SNA command). One of the major financial governance tests of 2018 will be the extent to which FGS can bring greater order and transparency to security sector expenditures.

More broadly, in spite of high-level political commitment to strengthening Government contracts, procurement capacity and understanding of procurement due process remains limited across Government. The majority of the expenditures submitted by FGS at the end of 2017 for reimbursement under the non-salary component of the World Bank's Recurrent Cost Reform Financing (RCRF) facility were deemed ineligible as agencies had failed to adhere to the required procurement processes. Close oversight and adequate capacity support will be needed going forward as individual FGS agencies continue to revisit old contracts

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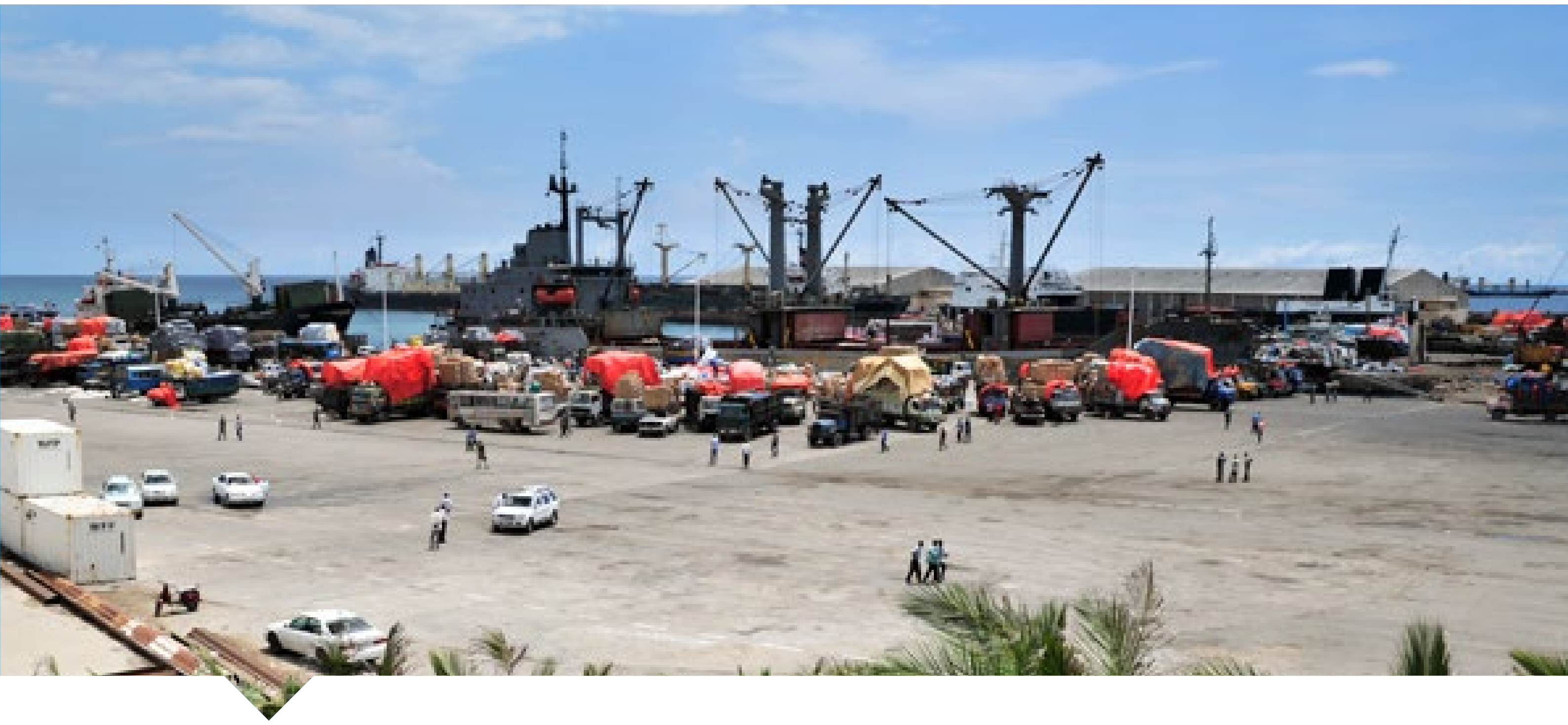


AU-UN IST PHOTO / TOBIN JONES.

and enter into new ones. Otherwise, there is a real possibility that past contracting mistakes will be repeated, in spite of there being a new legal framework for procurement through the 2016 Procurement Act.

In general, putting in place new legal frameworks and establishing appropriate policies only constitute initial steps towards stronger financial governance. Effective implementation is needed for these frameworks and policies to achieve their intended objective. In this vein, strong follow up will be required in order for the President's policy announcement on protecting public property to be implemented effectively.[9] Likewise, implementation of the 2017 Telecoms Law requires appropriate establishment of the Telecommunication Authority and its Board.

Although the level of dialogue between FGS and the FMS on fiscal federalism is encouraging, the current political momentum towards reaching a comprehensive agreement on revenue sharing between FGS and FMS needs sound technical underpinning. Given the limitations on data availability, and the substantial risks associated with inappropriately designed revenue sharing agreements, particularly in sectors such as petroleum, current efforts should focus on agreement on high-level principles, rather than percentage shares. FGS also needs to engage with individual FMS as they enter into agreements for major infrastructure redevelopments (e.g. ports) to avoid political confrontation, unhealthy competition and economic balkanisation.

9 https://www.hiiraan.com/news4/2018/Jan/146312/somalia_exploitation_of_public_land_is_barred_gov_t_assigns_national_committee.aspx

Fiscal Federalism

Progress	Challenges	FGC support and advice
■ Quarterly meetings between FGS and FMS MoFs instituted ■ Agreement on harmonisation of 'sin' taxes (khat, cigarettes) and international departure tax from 1st Jan 2018 ■ Agreement in principle to work towards harmonisation of sales tax ■ Over $28m of transfers made to FMS and BRA in 2017, funded by FGS own revenues, Saudi and Turkish budget support funds, RCRF and 'Surge support' ■ 2018 Budget provides greater transparency on planned transfers to individual FMS and BRA ($22.73m), in line with FGC advice	■ More work is needed to systematise transfers, particularly to provide an objective basis for their allocation across FMS, and between FMS and BRA ■ Greater transparency is needed with respect to transfer utilisation ■ Customs harmonisation remains a medium-term objective, but progress towards it can be made incrementally, for example by starting with agreement on adopting a common classification of goods in advance of transition from volume-based to value-based tariffs. ■ FGS has limited-to-no insight into high-value infrastructure agreements entered into by the FMS	■ FGC has participated in the regular meetings between FGS and FMS MoFs ■ Has provided advice on strengthening inter-governmental fiscal transfers in 2018. The FGC recommends that: ■ All transfers should be sent electronically direct from the TSA to recipients' bank accounts ■ FMS and BRA should provide basic reports to FGS on transfer utilisation ■ A clear set of criteria should be developed for 2019 transfer allocations

Natural Resources

Progress	Challenges	FGC support and advice
▪ Petroleum Bill has been submitted to Parliament ▪ Ministry of Petroleum has revised the Model Oil and Gas Production Sharing Agreement in line with FGC recommendations ▪ The PFM Bill that has been submitted to Parliament includes a section on natural resource revenue management, in line with FGC advice. It sets out procedures for banking and disbursing revenues, and provides for a natural resource revenue saving mechanism. ▪ In January 2018, President of FGS and the Presidents of the FMS came to an agreement on responsibility for fisheries licensing which paves the way for issuance of 2018 tuna licenses and a revenue sharing agreement.	▪ There is strong political momentum to arrive at a comprehensive agreement between FGS and FMS on revenue sharing in the coming months. ▪ While the momentum is positive, it requires sound technical underpinning. Given the limitations on data availability, and the substantial risks associated of inappropriately designed revenue sharing agreements, particularly in sectors such as petroleum, current efforts should focus on agreement on high-level principles, not percentage shares.	▪ FGC participated in the 2017 discussions on tuna licensing and prepared an advisory paper for FGS on international experience in natural resource revenue sharing in order to guide the way forward in Somalia. ▪ The paper and its presentation were translated into Somali and presented to the Economic Committee of Cabinet FGC advice has focused on: ▪ The risks of entering into agreements that are badly-designed or have not been sufficiently negotiated ▪ The importance of securing political agreement on the high-level principles guiding revenue sharing before entering into technical details at sectoral level ▪ The need for agreements to incorporate scope for future adjustment in light of changing circumstances

Recommendations from FGC Advisory Paper on Natural Resource Revenue Sharing

1 The Federal Government and the Federal Member States need to discuss and agree the *overarching principles* that will guide revenue sharing, before moving towards establishing individual sector-level agreements. Issues that require high-level agreement include: the balance between equitable revenue sharing and compensation to resource-rich areas and, the balance between immediate consumption of natural resource revenues and revenue savings.

2 Individual sector-level agreements need to identify which revenues arising from the sector are to be shared, how they are to be shared and the timeframe of the agreement.

3 A range of Federal Government Ministries should be involved in the revenue sharing discussions and negotiation of specific agreements. Given their importance for the fiscal federalism agenda, negotiations should not be left to individual agencies.

4 Revenue sharing discussions need to be appropriately synchronised with the Constitution re-drafting process. The Constitution should articulate the principles on which revenue sharing is based, but it is not advisable that it defines specific revenue shares or prescribes specific allocation mechanisms.

Domestic Revenue Mobilisation

Progress	Challenges	FGC support and advice
▪ FGS has started collecting revenues from new sources (e.g. sales tax) and was able to meet SMP revenue targets for end December 2017 and end March 2018. ▪ The PFM Bill that has been submitted to Parliament vests authority to grant tax exemptions solely in MoF, in line with FGC Advice. ▪ The Telecoms Act has been passed into law, paving the way for licensing and revenue generation from the sector. ▪ FGS has embarked on revenue reforms such as automation of non-tax revenue collections and establishment of large and medium tax payers' office (LMTO). ▪ Three contracts that were known to have concessioned non-tax revenue collections to private sector firms were determined to have failed to deliver value for money for the FGC and have been cancelled (road tax, property transfer tax, vehicle licensing) with revenue benefits to FGS. ▪ However, similar contracts issued by the previous administration have subsequently emerged (for work permits and visa issuance), and their status remains unclear. ▪ MoF has engaged the UN in order to commence revenue collection from UN contractors based at the airport who are not exclusively providing services to the Mission.	▪ FGS's decision to introduce sales tax on imported goods, as provided for in the 1984 Sales Tax Law, met considerable initial resistance from sections of the business community and from Parliament. One of the concerns cited was that imposition of the tax put traders in Mogadishu at a disadvantage to other areas of the country. ▪ Going forward, as FGS starts to develop updated Domestic Revenue legislation, it will need to ensure that there is thorough consultation with key stakeholders (business community, Parliament, FMS). ▪ It will also be important to secure FMS agreement on adoption of common provisions. ▪ Passage of the Telecoms Act does not automatically deliver objective and appropriate taxation of the Telecoms sector – supporting measures are needed to determine the dues owed by Telecoms firms and introduce new telecoms-related revenues.	▪ Several donors are involved in supporting FGS revenue mobilisation efforts. The FGC therefore mainly provides revenue advice on specific issues that do not fall under the purview of specific donor support projects. ▪ FGC has provided advice on the UN SOMA agreement, and the extent to which its terms can be strengthened to enable taxation of UN contractors ▪ FGC is providing advice to FGS on best practice with respect to the taxation of donor-funded activities ▪ FGC continues to provide advice on all FGS concessions that have a revenue component, and monitors their revenue performance ▪ FGC is encouraging FGS to hold discussions with ICAO and the UN regarding reimbursement of Somalia's historical overflight charges

Public Procurement and Concessions

Progress	Challenges	FGC support and advice
■ With FGC/ALSF/World Bank support, FGS is working towards renegotiating the Al Bayrak port concession and Favori airport concession. The objective is to secure clearer contract terms and agree performance standards. ■ Renegotiation of the Al Bayrak port concession is expected to enable an agreement on the way forward for the Simatech dry port concession. ■ FGS is also in the process of renegotiating the Sahel airport shuttle concession. ■ H.E. the President has placed a moratorium on the disposal of public property. ■ The Council of Minister's Economic Committee has approved interim procurement requirements to guide public procurement until such a time as the Procurement Act is fully implemented, in line with FGC advice	■ The SNA rations contract that had been competitively tendered by the previous administration was cancelled and re-awarded without due process by the SNA Command in April 2017. The MoF conducted a legal review which determined that the cancellation and re-award was irregular, and the Economic Committee resolved that the contract should be retendered. However, the decision has not yet been implemented. ■ Work is needed to address several contracts entered into by the previous administration on a sole source basis without adequate scrutiny (passports, visas, prison rations) ■ Sole source contracting for goods and services between $2,000 - $50,000 (as opposed to soliciting 3 quotations) was a major reason for FGS's failure in 2017 to meet RCRF NSRC reimbursement requirements ■ There remains a risk that individual FGS agencies will award high-value contracts and concessions on a sole source basis without following established procedures or oversight from the INPB ■ The Procurement Act, once fully implemented, will establish a highly decentralised procurement system, whereby ministries will be able to procure contracts of any value and to use non-standard bidding methods such as sole-sourcing without third party approval	■ FGC continues to provide active support to enable FGS to move towards renegotiation of the Favori & Al Bayrak contracts, most recently helping prepare MoUs to govern the terms and timelines of the renegotiations ■ FGC has continuously flagged the need to retender the SNA rations contract on a transparent and competitive basis ■ FGC continues to provide advice on other FGS contracts that require renegotiation (e.g. airport taxi contract) and to request documentation on reported public property disposals ■ FGC advised on the need to establish interim procurement requirements until such a time as the Procurement Act is fully implemented, and continues to highlight the need for adequate capacity building and oversight in the meantime ■ FGC has presented an advisory report to FGS proposing immediate steps to strengthen the Protection of Public Property (immoveable assets), providing a platform for implementation of the President's moratorium on the disposal of public property ■ FGC has provided advice on possible amendments to the 2016 Procurement Act, to enable contract awards above a certain value to be subject to approval by a third party within Government

Expenditure Management

Progress	Challenges	FGC support and advice
▪ Police officers' salaries and cash allowances for fresh rations ('idaan') are being paid direct to individuals' bank accounts ▪ FGS has initiated a pilot for SNA personnel registration and salary payment direct to bank. Just over 5,000 personnel have been registered so far, and their details entered into the payroll module of SFMIS. Payment of their salaries direct to bank is due to start in May 2018. ▪ FGS has started using the Purchasing Module in SFMIS as a first step towards controlling contractual commitments in line with budget availability ▪ The PFM Bill has been submitted to Parliament	▪ Significant amounts of security expenditures across all forces continue to be paid to the agencies own bank accounts; the only non-wage expenditures currently paid direct to suppliers are the rations contract payments. ▪ NISA and Prisons rations contracts continue to include a cash component for fresh rations ('idaan'). This means that the contractor delivers a cash sum equivalent to $30 per person per month to the NISA and Prisons leaderships. ▪ SNA allowances for 'idaan' are paid direct by MoF to the SNA and released to unit commanders, rather than paid to individual personnel. ▪ Donors supporting payment of SNA stipends do not make use of FGS systems. FGS's initiative of registering security sector personnel and paying them direct to their accounts provides an opportunity to discuss the harmonisation of stipend payments with FGS systems.	▪ FGC continues to closely monitor FGS progress in reforming security sector salary payments, with the objective that salaries and allowances for fresh rations ('idaan') are paid direct to individuals' accounts ▪ Given that FGS spends almost $1m per month/$12m per annum on security sector dry rations, FGC has provided advice on strengthening rations delivery verification mechanisms, to ensure that FGS only pays for what it receives.

Financial Sector Development and Asset Recovery

Progress	Challenges	FGC support and advice
■ First phase of currency reform, covering issuance of smaller value notes (1000, 2000, 5000 and 10000 shillings) planned for 2018. Decision on the currency conversion factor will be made in advance of the first phase. ■ The second phase of currency reform will cover the issuance of larger denomination notes (20000 and 50000). A decision on the exchange rate regime will be taken at this juncture. ■ FMS have provided written commitment to prevent/combat counterfeiting in their jurisdictions ■ Working with the World Bank StAR programme, and with advice from FGC, FGS has recovered over $1m in frozen assets from banks abroad	■ The FGS will need to raise $41m from the donor community to cover the cost of the first phase of currency reform ■ The second phase of the currency reform requires significant preparatory work, including strengthening the CBS's institutional capacity and developing independent monetary policy instruments and reserve management guidelines.	■ FGC continues to closely monitor FGS progress, and provide pertinent advice, in implementing the currency reform road map ■ FGC continues to provide active support to FGS asset recovery efforts in conjunction with the WB STAR programme, and has acted as a conduit to further help FGS identify previously unknown legacy assets ■ FGC advised on AML/ CFT bill and its implementation. ■ FGC to monitor development of the financial sector roadmap.

Access to Financing

Progress	Challenges	FGC support and advice
▪ FGS secured $70m in additional budget support financing for 2017 and 2018 from Saudi Arabia and Turkey ▪ The World Bank provided $6m of additional financing through RCRF in 2017 to enable FGS to provide 'Surge' support for infrastructure and youth employment to FMS/BRA. A further tranche of $13m is expected in 2018 contingent on the attainment of a number of policy reforms. ▪ EU stipend payment support for Police is now routed through the FGS Treasury, although UNOPS maintains the paylist and issues the payment instructions. ▪ The EU has committed to providing Euros 100m in direct budget support to FGS ▪ FGS is making progress towards achieving debt relief by building a strong track record of economic and financial development and meeting IMF/SMP requirements.	▪ The overall level of direct external financing to FGS remains low. Only 8% of development aid was delivered on treasury in 2016, against a target of 15%. For 2017, the percentage improved considerably to 14%*, but remains below target, while the target itself is extremely modest.	▪ FGC provided inputs to the Use of Country Systems working group report on the risks and benefits of using country systems ▪ FGC advised on various reforms with partners to build track record in the context of the SMP ▪ FGC has advised FGS to treat external untied grants with the same oversight and transparency as regular budget funds

* https://s3.eu-central-1.amazonaws.com/somalia-aid-flows.so/Aid+Flows+in+Somalia+-+2018FINAL.pdf

Financial Governance priorities in the coming year

Through mechanisms such as the IMF programme and the Mutual Accountability Framework (MAF)[10], FGS has agreed a number of targets with the international community which aim to strengthen its economic and fiscal capacity and develop its public financial management system. Sound public finances underpin legitimacy and stability and are crucial to maintaining peace and a long term political settlement. It is widely acknowledged that developing institutional capacity can take years[11], and some of these targets are medium to long-term in nature.

The FGC's focus is on the financial governance actions the FGS needs to take in the short term to support its state building agenda and demonstrate its continued commitment to reducing the scope for mismanagement of public resources. The FGC's top ten priorities for 2018 therefore focus on strengthening fiscal federalism, enhancing transparency in contracting and asset disposal, mobilising revenues and reducing the use of cash in the execution of government expenditures.

10 https://www.gov.uk/government/publications/new-partnership-for-somalia-for-peace-stability-and-prosperity

11 World Development Report 2011: Conflict, Security and Development, World Bank

These actions are not purely technical in nature. Their effective implementation will be contingent on political commitment at the highest level; increased Federal Government capacity to work effectively with the Federal Member States on an agreed financial governance agenda; increasing co-ordination between individual federal agencies; a continued culture shift away from legacy practices such as sole-source contracting; and, outreach to the business community.

Financial governance issues should also have a special place for discussion in the ongoing constitutional discussions focusing on fiscal federalism and resource sharing.

Top ten Financial Governance priorities in the coming year

1 Complete registration and payment to bank of all security sector personnel, including cash for fresh rations ('idaan')

2 Re-tender SNA and Prisons rations contracts in line with interim procurement requirements and establish a strengthened rations delivery verification mechanism

3 Re-negotiate Port (Al Bayrak) and Airport (Favori) concessions, and resolve other outstanding legacy contracts from the previous administration (Sahel Airport Shuttle, Simatech Dry Port, Passports, Visas)

4 Ensure all new procurements of contracts and concessions are conducted in accordance with the interim procurement requirements

5 Reach an agreement between FGS and Federal Member States on the principles underpinning revenue sharing

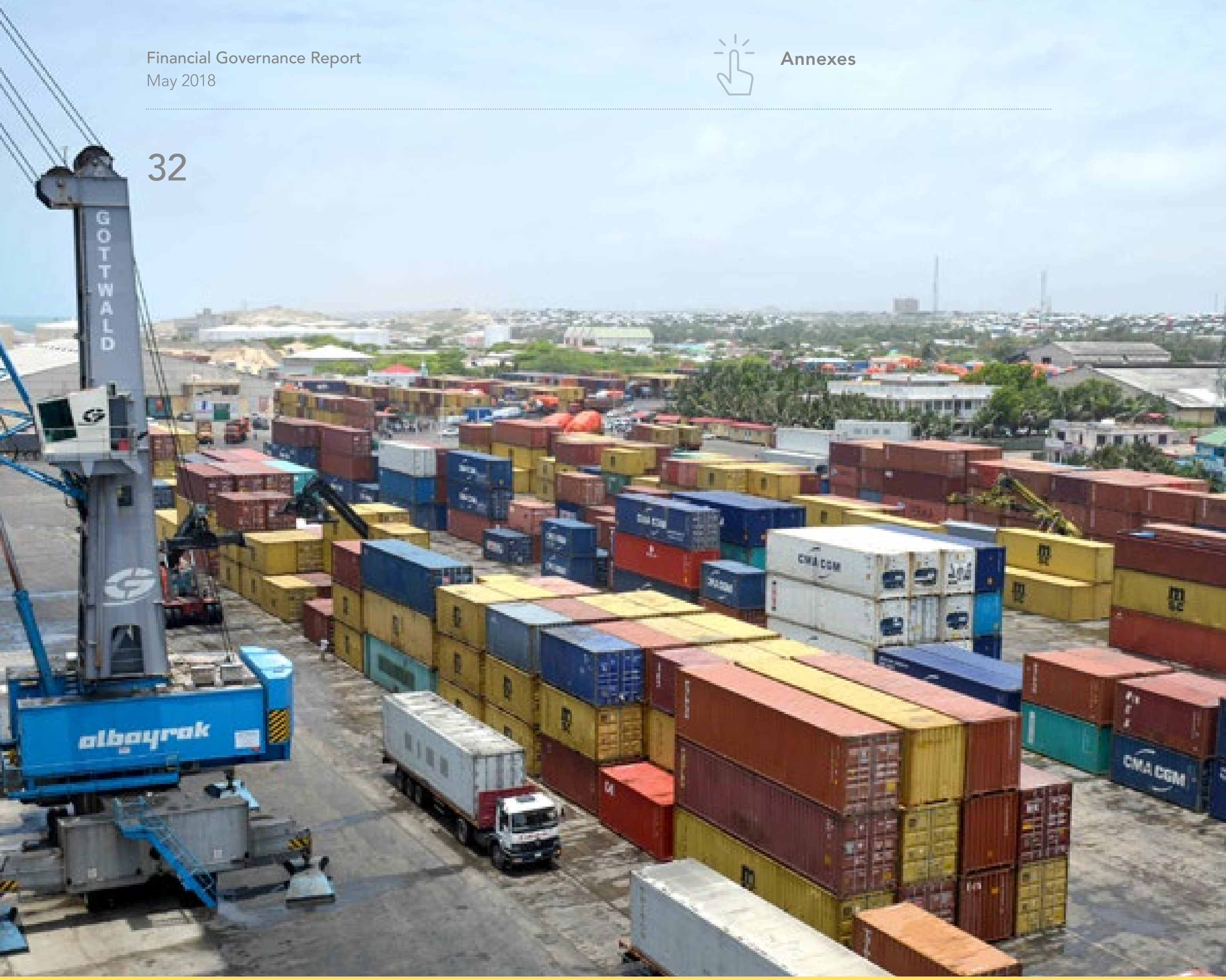
6 Modernise the legislative and administrative framework for inland revenue in consultation with Federal Member States and business community

7 Agree a Customs Modernisation Plan with the Federal Member States which includes a roadmap for from transitioning from volume-based to value-based customs tariffs

8 Institute basic reporting on transfer utilisation and agree an objective basis for 2019 transfer allocations to Federal Member States and Banadir

9 Compile a full inventory of Federal Government property and begin to review all public property leasing and disposals since 2012

10 Implement the first phase of currency reform



Annexes

Annex 1
List of contracts and concessions reviewed by the FGC since 2014

#	FGS Agency	Contract	Contractor	FGC Official Review	Status
1	Central Bank of Somalia	Land lease and redevelopment	Riverside Holding	2016	On hold
2	Central Bank of Somalia	Asset recovery	Shulman, Rogers, Gandal, Pordy & Ecker PA	Not required	Cancelled
3	Commerce and Industry	Import/export quality assurance	Proje Gözetim Mühendislik (PGM Project)	2015 and 2016	Operational - incorporated FGC recommendations
4	Defense	SNA Rations	AGETCO	2016	Contract cancelled
5	Defense	SNA Rations	AGETCO	2017	Contract awarded following a tender under the oversight of INPB; subsequently cancelled
6	Defense	Supply of 6 marine patrol boats	AMO Shipping Company Ltd.	2014	Did not proceed
7	Defense	Equipping and training Coast Guard	Atlantic Marine and Offshore Group	Not required	Did not proceed
8	Defense	SNA Rations	Kasram	2017	Economic Committee has recommended cancellation and retendering.
9	Finance	Collection of property transfer registration tax	M&T Solutions Ltd	2016	Cancelled
10	Finance	Collection of road tax	Smart General Service Ltd	2016	Cancelled
11	Finance	Khat tax collection on behalf of FGS	The ADCO Group of Companies	2015	Cancelled -Contract replaced by direct tax
12	Fisheries and Marine Resources	Protecting, licensing, policy and institutional development of fisheries sector	Somalia-FishGuard Ltd.	2014	Did not proceed

#	FGS Agency	Contract	Contractor	FGC Official Review	Status
13	Galmudug Regional Government	Oil production sharing agreement	Petro Quest Africa (CN)	2014	Did not proceed
14	Interior	Police rations	Perkins Logistics	2016	Operational – partially incorporated FGC recommendations
15	Internal Security	NISA rations	Horn Logistics	2016	Operational – partially incorporated FGC recommendations
16	Internal Security	Scanning services for Mogadishu Port	M&T Solutions Ltd	2016	Recommended to be retendered. Status unknown
17	Justice	Prisons Rations	Bakhaari Logistics	2018	Operational. Recommended to be retendered
18	Petroleum and Mineral Resources	Establish model terms for petroleum exploration, development and production	Model Oil and Gas Production Sharing agreement	2016	Incorporated FGC recommendations, pending final endorsement
19	Petroleum and Mineral Resources	Seismic data analysis	Mubadala Oil and Gas Holding Company LLC (CN)	2015	Agreement Expired
20	Petroleum and Mineral Resources	Seismic Exploration	Soma Oil and Gas Exploration Limited	2014	Operational - did not incorporate FGC recommendations
21	Petroleum and Mineral Resources	Geospatial Analysis	CGG Data Services AG/Robertson GeoSpec International Ltd.	2014, 2015 and 2016	Operational - incorporated FGC recommendations
22	Petroleum and Mineral Resources	Collation, analysis and marketing of petroleum data	Spectrum ASA	2015	Operational - incorporated FGC recommendations
23	Petroleum and Mineral Resources	Acquisition, processing and marketing of geophysical data	TGS-NOPEC Geophysical Company ASA	2014	Did not proceed
24	Ports and Shipping	Management of Port Operations	Albayrak Turizm Inşaat Ticaret A.Ş.	2014	Operational - under renegotiation

#	FGS Agency	Contract	Contractor	FGC Official Review	Status
25	Ports and Shipping	Harbour, fishing port and related infrastructure developments	Great Horn Development Company	2014	Did not proceed
26	Ports and Shipping	Lease and concession for operating Mogadishu port container terminal	Mogadishu Port Container Terminal and Simatech International	2014	Did not proceed
27	Ports and Shipping	Management and operation of a container yard and freight station at Mogadishu Dry Port	Mogadishu International Port and Simatech International	2016	Construction complete, not yet operational
28	Posts and Telecoms	Telecoms gateway	VBH Holdings SPA	2016	Did not proceed
29	Power and Water	Electricity generation	Polaris Energy SDN BHD	2015	Did not proceed
30	Transport and Aviation	Airport Operations	Favori LLC	2014	Operational – under renegotiation
31	Transport and Aviation	Vehicle licensing	Modern Technology Ltd	2016	Cancelled
32	Transport and Aviation	Airport taxi shuttle service	Sahel	2017	Operational - under renegotiation
33	Transport and Aviation	Airport Hotel	Sat Service LLC	2018	Draft contract under review

Annex 2
Progress in implementing 2017 FGR recommendations

Achieved | Some Progress | No known progress/ not implemented

Fiscal Federalism		
Recommendations		Progress
1	Establish an initial agreement on revenue authority, expenditure responsibility and mechanisms for resource equalisation in advance of any Constitutional Settlement, with technical details developed with counterparts at FMS level	Communiqué between FGS and FMS on 5th November 2017 agreed the establishment of a Task Force to develop a consensus on Federal Affairs in 6 months
2	Establish an office responsible for coordinating the federalism agenda in either the Presidency or the Prime Minister's Office	Office expected to be established to provide logistics and advisory support to the OPM Tech Committee, and wider federalism dialogue structure. However, the exact nature, scope and institutional location of that office are not yet fully defined
3	Agree on harmonised customs tariff with FMSs while awaiting political agreement on broader principles	Agreement reached on 27 September 2017 to harmonise tariffs for cigarettes, khat and departure tax. Agreement in principle in Dec 2017 to work towards harmonising sales tax. No substantive discussion on customs.
4	Support inter-governmental fiscal system by aligning national and subnational fiscal arrangements and making small transfers to the FMSs on a regular basis	During 2017, FGS made transfers to FMS and BRA through two different FGS Agencies; the Ministry of Finance and the Ministry of Interior and Federal Affairs. These transfers used different budget and transfer mechanisms and drew on different funding. Overall, FGS transferred USD 28.7m to FMS and BRA during Fiscal Year 2017.
5	Donors need to inform FGS of the support they are providing to FMSs and involve FGS in project design to ensure it aligns to the agreed fiscal federalism principles.	

Transparent and Equitable Management of Natural Resources

Recommendations		Progress
1	Finalize the revisions to the legal framework for petroleum and establish the necessary regulatory institutions before entering into any production sharing agreements.	The Petroleum Bill was submitted to Cabinet for approval. Cabinet has subsequently approved the Bill and submitted it to Parliament.
2	Approve the finalised model Oil and Gas PSA in line with FGC recommendations at Cabinet level	Model Oil and Gas Production Sharing Agreement was reviewed by the FGC in December 2016 and the draft was revised by Ministry of Petroleum in February 2017 in line with FGC comments. Ministry of Petroleum to finalize/adopt the Model PSA.
3	Base discussions of specific PSAs on finalized model PSA, which should also be approved by the INPB and by Cabinet	Not yet applicable (no individual PSAs known to be under discussion)
4	Insert clauses in the draft PFM Bill that set out the principles governing natural resource revenue management as relates to fiscal policy.	The PFM Bill that has been submitted to Parliament includes a section on natural resource revenue management. It sets out procedures for banking and disbursing revenues, and provides for a natural resource revenue saving mechanism.
5	Agree a framework for sharing 2017 federal offshore fishing license revenues with FMSs, and use the inter-governmental fiscal transfer system to provide FMSs with their shares in a way that creates incentives for licensing compliance.	An agreement between the Federal Government and Federal Member States on an interim process for fisheries licensing was reached for 2018.
6	Review the revenue sharing formula proposed in the petroleum agreement, and initiate new negotiations with all FMSs.	FGC has shared advisory note to guide new discussions

Domestic Revenue Mobilization

	Recommendations	Progress
1	Conclude renegotiations of all five existing revenue collection contracts before the end of 2017, establishing clearer contract terms and ensuring stronger oversight of their revenue streams going forward.	3 contracts were cancelled, following a determination that they did not offer value for money (property transfer tax, road tax, and vehicle licensing). 2 are under renegotiation (port and airport)
2	Provide guidance to counterparts in the FMSs on how to develop and manage revenue collection contracts based on its own experience.	
3	Insert a clause into the PFM Bill stating that the power to grant tax exemptions will be vested solely in the Minister of Finance. FGS should seek to minimise the tax exemptions that it offers in its contracts and concessions, given the negative precedent such an approach sets for future tax and contract negotiations.	A clause was included stating "The Minister has the sole authority to exempt a tax or fee or charge provided for any exemption over the value prescribed in regulations, the Minister has obtained the prior approval of the Council of Ministers"
4	Political level commitment is needed to tax compliance and passage of relevant legislation (e.g. Communications Act).	ICT Act was passed by Parliament and signed into law.
5	Initiate dialogue with the private sector to secure their commitment to meeting their legal tax obligations and gain an understanding of the services they need to provide in return.	The MoF has held substantive dialogue with banks, money transfer agencies, Turkish Airlines, telecoms, cable television providers, electricity providers, and water providers, in advance of the collection of sales tax.

Credible Public Procurement and Concessions

	Recommendations	Progress
1	Issue a Prime Ministerial Decree re-affirming its commitment to due process in contracting, concessions and asset leasing. The Decree should: specify procurement roles and responsibilities within FGS until such a time as the Procurement Act can be adequately implemented; extend the mandate of the INPB for the duration of the transition period; set out the steps all draft agreements must follow prior to signature; and, state the consequences of non-compliance.	Interim procurement requirements were approved by the Economic Committee of Cabinet in December 2017 and disseminated to all spending agencies by the Ministry of Finance.
2	Assign responsibility for contracting all FGS goods and services above a certain threshold to the Ministry of Finance's Procurement Unit as an interim measure until procurement units in line ministries have the necessary capabilities.	Covered under the Interim Procurement Requirements
3	Donors need to step up their support to FGS procurement; significant levels of operational support and capacity building are required both within the Ministry of Finance and across line ministries.	
4	Support the continuation of the recently established Commission to Protect Public Properties, working to a clear, expanded terms of reference.	In mid-2017, FGC prepared a report with recommendations on how the government could immediately prevent the further loss of public land and property and protect existing public land and property in Somalia. The report was discussed by the Economic Committee of Cabinet in December 2017. The President announced in January 2018 that a Committee would be formed to Protect Public Property.

Strengthened Expenditure Management

	Recommendations	Progress
1	Provide explicit backing to the Ministry of Finance to further reduce the proportion of the non-wage payments that are paid out in cash, and to require all advances to be fully accounted for before new ones are made.	There has been an increase in the amounts being paid directly to vendors since the 4th quarter of 2017
2	Place much stronger controls on the payroll, as otherwise gains made in increasing revenue and reducing funds leakage will be fully absorbed by a rising wage bill.	Draft Report on Establishment Control supported by World Bank, reviewed by FGC. Civil Service Law drafted and approved by Cabinet
3	Establish an Inspection Function responsible for verifying the delivery of goods and services above a certain value prior to the payment of invoices.	Under initial discussion with respect to rations
4	Complete the process of cleaning and consolidating the SNA payroll and undertaking biometric registration of personnel, and commence payment of salaries (and rations cash) direct to in individuals' accounts.	FGS has initiated a pilot for SNA personnel registration and salary payment direct to bank. Around 5,000 personnel have been registered so far, and their details entered into the payroll module of SFMIS.
5	Donors providing stipends to the security sector should commit to becoming part of the SNA payroll and payment reform; the objective should be that all SNA salary and stipend payments are made against a single, commonly agreed payroll and paid direct to individuals' accounts through the FGS system, as already occurs with the Police.	Commitment made by both parties in MAF to plan for payroll consolidation and verification, transition to electronic payments and establishment of effective HRM systems for SNA and federal police agreed by National Security Council

Financial Sector Development

	Recommendations	Progress
1	FGS to hold discussions with the FMSs to come to a clear, common understanding of the role of the CBS in the regions in the context of the broader fiscal federalism discussions, and with respect to currency reform.	CBS initiated discussion in the context of the currency reform and re-opening of its regional branches. FMS have signed undertakings to prevent counterfeiting in their jurisdictions
2	FGS and CBS should hold discussions in order to develop a mutual understanding of the key choices and risks associated with currency reform	MoF and CBS have discussed approach to currency conversion. Exchange rate regime will be determined during the second phase of currency reform
3	Particular attention needs to be paid to the issue of currency conversion, to ensure that currency reform does not have a negative impact on people with low incomes who currently hold old Somali shilling notes.	CBS preference is for full conversion to mitigate this risk
4	Successful completion of the currency reform will require substantial donor financing, for printing and distributing the new currency, plus any costs of converting old notes for new ones.	

Access to External Financing

	Recommendations	Progress
1	FGS and its creditors should develop a milestones-based debt relief roadmap setting out how Somalia can qualify for the HIPC debt relief process. As a part of this, FGS and the IFIs should reach an agreement on the adjustments they need to make to the NDP so it can qualify as a poverty reduction strategy paper (PRSP).	FGS is on track with implementation with the second SMP. A third SMP is due to commence in May 2018. Subject to board approval, the World Bank will provide pre-arrears clearance financing to FGS in 2018-19.
2	FGS should use the London conference as an opportunity to make the case to the international community of the benefits of increasing direct grant financing, and the risks of not doing so.	The London Conference on Somalia took place at Lancaster House on 11 May 2017, co-chaired by the UK, the Federal Republic of Somalia, the United Nations and the African Union, and attended by 42 partners of Somalia. FGS made the case for increased direct financing.
3	FGS and donor partners should revise the current 15% target for development aid on budget and make it more ambitious.	Less than 15% of development aid currently channeled through the FGS Treasury
4	FGS and donors should use their forthcoming joint 'risk-benefit analysis' of the use of country systems to identify concrete risk-mitigation actions that they can implement to support the scale-up of aid through FGS.	Use of Country systems report contains guidance on the risks and benefits of using country systems in Somalia
5	FGS should hold discussions with interested IFIs on the potential scale and role of blended finance in Somalia.	
6	The international community should help expand government engagement with the HRP, by strengthening reporting to FGS on how HRP funds are spent, both sectorally and geographically, and by whom.	

Financial Governance Report

Financial Governance Committee

May 2018