



THE FEDERAL GOVERNMENT OF SOMALIA

**RCRF II PROGRESS REPORT AND FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30st, 2017**

**RECURRENT COST AND REFORM FINANCING PROJECT –
PHASE II (P154875, TF0A0534)**

30th June, 2017

The Federal Government of Somalia
 Progress Report on Recurrent Cost & Reform Financing (RCRF) Project – Phase II
 (P154875, TF0A0534) for the Period ended on June 30th, 2017.

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INTRODUCTION

This report presents the implementation status of the Recurrent Cost and Reform Financing Project (RCRF II) at the end of the fourth quarter of the 2015 financial year through third quarter of 2016 fiscal year. The project has registered a number of achievements over this reporting period. The project will be completed at the end in June 2020.

This report presents the Progress, Financial and implementation status of the Recurrent Cost and Reform Financing Phase II Project (RCRF II) since the project became effective on July 2nd 2015 through Dec 31, 2016. The strategic goal of this project is to support operational payroll expenditures that enable Federal Government of Somalia to pay salaries of Non-security sector employees and other Non-salary recurrent costs. The Phase I Recurrent Cost and Reform Financing (RCRF) project has been the first MPF grant to be operational, and reflects the particular and emergency conditions that are facing the Federal Government at this sensitive point in the Somali transition period. The program is prepared as a phased program (Series of Projects).

Phase one for US\$16 million and for eight months from August 20 to April 30, 2015 (As extended from six months), with retroactive financing from July 2014 for civil service salaries. With same of objective of RCRF I, The RCRF Phase II project's development objective is to support an operational payroll and payment system for the non - security sectors and contribute to the credibility and legitimacy of the federal government of Somalia. Project allocated 39 million for 2015-2016, where by 21.4 million of actual expenses out of 39 is allocated for Civil Servant Non-Security sector employees in Mogadishu as of December 31, 2016; thus project is still using 2015-2016 budget due to number of budgeted activities, but has not been implemented as it was planned for. However, in quarter 1, of 2017, actual payroll expenses amounts \$1.5 million where total actual of payroll expenses funded by project from the inception to Mach 31, 2017 is 22.9 million.

Project Scope:

The World Bank has established a Multi-Partner Fund (MPF) to provide development support to the transition in Somalia, with an early focus on supporting the Federal Government to re-establish basic functionality. The MPF is the Bank-administered window of the broader SDRF, working alongside the UN Multi-Partner Trust Fund. The SDRF thus brings together the UN and World Bank in a close collaboration with common governance, reporting and risk management. Designed to consolidate donor funding under government leadership and accountability, the SDRF makes the most of the comparative advantages between the two multilateral institutions, ensuring rapid response as well as longer-term development and institution-building needs are met. In the second phase of its work (July 2015 – June 2020), the MPF planned to finance a set of institutional support grants while preparing for larger investments in economic foundations, notably both urban and rural infrastructure projects.

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The Phase I Recurrent Cost and Reform Financing (RCRF) project has been the first MPF grant to be operational, and reflects the particular and emergency conditions facing Federal Government at this sensitive point in the Somali transition. The program is prepared as a phased program (Series of Projects). Phase one for US\$16 million and for eight months from August 20 to April 30, 2015 (As extended from six months), with retroactive financing from July 2014 for civil service salaries. This lean strongly on government budget and about seventy percent is in respect of payments of salaries to civil servants and subject matter experts in Mogadishu. The whole amount of US\$16 million of the Grant Agreement has been signed. Phase II is the continuation of phase I with the Budget of 39 Million for 2015-2016, thus, for the time being, project activities are funded from 39 million.

PROJECT INFORMATION

The RCRF project's development objective is to support an operational payroll and payment system for the non-security sectors and contributes to the credibility and legitimacy of the federal government of Somalia. The project is implemented under four project components:

Component 1: Support to core government functions of ministries, departments and agencies in FGS (US\$81.0 million).

Component 2: Inter-governmental fiscal transfers to core government functions of eligible federal member states, interim and emerging administrations (US\$34.0 million).

Component 3: Support of recurrent costs in health and education sectors in FGS and eligible member states, interim and emerging administrations (US\$20.0 million).

Component 4: Project management and coordination (US\$9.0 million).

Component 1.1. Financing of Eligible Civil Service salaries in non-security sectors in FGS

Financing of salaries of non-security sector civil servants is based on a declining scale over the project implantation with the objective that these would be phased out by the end of project when the government will ultimately finance all civil salary payment from its domestic revenues. Its defined development objectives include supporting the government to provide credible and sustainable payroll and to establish the foundation for efficient budget execution and payment systems for the non-security sectors in FGS and eligible member states as well emerging ones.

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In March and April 2015, project paid U\$1,600,000 for salaries of Non- Security sector employees for each month, which is 76% of payroll expenses for civil servants. In May payroll expenses, project had contributed U\$1,500,000 that has covered 71% of overall payroll expenses for Non – Security sector in Mogadishu. In June payroll expenses, project has contributed \$1,400,000, which is covered 66% of payroll expenses. July and August payroll expenses have been paid in Quarter 4 2015 and project has contributed \$1,400,000 and \$1,300,000 respectively where 62% and 57% were covered by project contribution to payroll expenses. September-October 2015 salaries were arrears budgeted in 2016 fiscal year and have been paid in Jan 2016 where RCRF II project has paid \$2,300,000 out of \$4,235,356 which is covered 57% and 52% of payroll expenses respectively.

In 2016 salaries, FGS paid January, February, March, April, May, June, July, and August 2016 salaries; where November-December 2015 salaries are also yet to be cleared. FGS has challenges in collecting revenues and payment of civil servant salaries is an obligation needs to be met by FGS. From the inception of the project, in overall civil servants payroll expenses in total of \$47,219,417, project has paid \$25,776,145, which covered 54.58% of salaries cost in 2015-2017. Salaries of September, October, November and December of 2016 were not cleared as of this report. However, government paid January 2017 salaries in February 2017.

Below table depicts payroll analysis from March 2015 to Jan, 2017 for Non-Security Sector employees in Mogadishu; subsequently, project will pay U\$1,500,000 in next payroll expenses and project contribution will remain One million Five Hundreds Thousands for each month in 2016. Project has paid \$1,500,000 out of \$2,603,360 of Jan 2017 payroll expenses. In quarter II 2017, payroll expenses paid amounted \$8,167,685 where project has contributed \$2,876,145 out of amount mentioned above. Following a request from the Government The Bank agreed to revise the sliding scale process.

RCRF Phase II Civil Salaries Payments from March, 2015 to April, 2017

Date	Civil servants presented to CBS for payment						No. Civil Servant paid in first 10 days at CBS	Staff who did not claim their salaries	
	No.	Amount paid US\$	Date payment Starts	Amount WB paid	% WB Paid	% FGS Paid		No.	US\$
Mar 2015	4,095	2,101,192	13-July 15	1,600,000	76%	24%	3,923	172	101,681
Apr 2015	4,085	2,100,486	22-July 15	1,600,000	76%	24%	3,903	182	104,726
May 2015	4,097	2,107,878	01-Aug 15	1,500,000	71%	29%	3,906	191	114,406

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June 2015	4,094	2,105,920	30-Sept 15	1,400,000	66%	34%	3,881	213	125,470
July 2015	4,083	2,101,844	26-Oct 15	1,300,000	62%	38%	3,883	200	119,926
Aug 2015	4,101	2,109,609	15- Dec 15	1,200,000	57%	43%	3,895	206	123,759
Sep 2015	4,110	2,117,678	20- Jan 16	1,200,000	57%	43%	3,955	155	96,099
Oct 2015	4,110	2,117,678	20- Jan 16	1,100,000	52%	48%	3,954	156	96,834
Jan 2016	4,329	2,319,994	10- Mar16	1,000,000	43%	57%	4,186	143	89,683
Feb 2016	4,376	2,346,002	19- Apr 16	1,000,000	42%	58%	4,376	0	0
Mar 2016	4,397	2,356,903	11- June16	1,000,000	42%	58%	4,397	0	0
Apr 2016	4,545	2,447,645	10- July16	1,500,000	61%	39%	4,545	0	0
May 2016	4,635	2,490,483	14-Aug16	1,500,000	60%	40%	4,635	0	0
June 2016	4,672	2,519,324	06-Oct 16	1,500,000	59%	41%	4,672	0	0
July 2016	4,690	2,532,414	13-Nov 16	1,500,000	59%	41%	4,690	0	0
Aug 2016	4,771	2,573,322	22-Dec 16	1,500,000	58%	42%	4,771	0	0
Jan 2017	4,827	2,603,360	14-Mar 17	1,500,000	58%	42%	4,827	0	0
Feb 2017	4,849	2,621,245	04-Apr 17	1,500,000	57%	43%	4,849	0	0
Mar 2017	4,901	2,648,153	02-May 17	684,310	26%	74%	4,901	0	0
Apr 2017	5,127	2,898,287	25-May 17	691,835	24%	76%	5,127	0	0

Component 1.2 Financing of Salaries and allowances to Government staff and young graduates recruited under the Capacity Injection Mechanism (CIM)

This sub-component is financing salaries and allowances of a cadre (525) of critical advisory, managerial and technical staff to fill urgent staffing gaps identified by FGS through the Capacity Injection Mechanism (CIM). This includes salaries and allowances of a number of young graduates who are expected to be absorbed into the civil service. Core government functions that will be strengthened include (i) policy and strategy management (planning, implementation and M&E); (ii) financial management (budgeting accounting and auditing); (iii) procurement management; (iv) revenue mobilization and; (v) human resource management. We need to paraphrase this - ten pilot beneficiary institutions were identified in FGS while 9 were picked up in Puntland Beneficiary institutions and eligible positions will be selected instead of identified with the support of the World Bank and UNDP capacity Injection projects on the basis of agreed criteria.

The financing of a cadre salary has fully commenced in the beneficiary institutions of the project that started recruiting skilled staff under this sub-component. These institutions include Office of the Prime Minister, Office of the President, Ministry of Finance, Ministry of Planning and International Cooperation, Ministry of Energy, Ministry of Agriculture, Ministry of Labor and Social Affairs, Ministry of Public Work, Central Bank

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of Somalia and National Civil Service Commission. The project financed salaries of these institutions from March 2016 onwards. Financing of those newly injected staff across several other MDAs will be going in coming quarters of 2016. However, it is worth mentioning that CIM salaries were budgeted under the respective institutions and MDAs request payment by submitting signed individual contracts and approved timesheets to the EAFS for processing salaries. So far 51 individuals including CIM Coordinator have been recruited and placed in across the pilot institutions. Salaries for three months from March to May 2016 have been paid from project fund to those recruiters. All other CIP cadres who have been recruited are paid from project funds with MDAs budget allocation except Central Bank of Somalia staffers who have budget under the project.

FGS is committed to scale up recruiting skilled staff under this subcomponent to inject capable and professional staff across all MDAs. The number that has already been recruited would be integrated into the SFMIS.

Sub-Component 1.3 Non-Salary Recurrent Cost for Selected MDAs

Claiming of Non Salary recurrent costs for MDAs started at slow pace. First \$2,000 of non-salary recurrent cost expenses incurred and paid was claimed on Withdrawal Application 2. EAFS office recently received \$5,000 non-salary recurrent cost documents from Office of the Accountant General and has sorted them out for processing and handed over to Monitoring Agency for further review. 59 copies of supporting documents have been forwarded to MA for the USD 5,000 expenditure only. However, Monitoring Agency has released their opinion and report, where \$1,680 out of 5,000 has been approved as eligible expenses. One single penny above the said threshold (1,999.99) caused ineligibility of \$2,000 eligible expenses. The difference of 1,320 remains ineligible due to expiration date of Business registration for vendor.

Due to long list of eligibility criteria and conditions set-forth, where most of forms required have same and duplicate information on, the processing of a number of NSRC expenses are still pending for monitoring agency approval. The design of the eligibility criteria makes the work flow inefficient. If monitoring review procedural requirement remain intact and current circumstance on non-salary recurrent cost reviews remains unchanged, this sub-component will most likely continue to be under utilized.

Current eligibility criteria and difficulties in meeting certain conditions by the MDA on non-salary recurrent expenditures make the reimbursement processes almost impossible. The need for a TSA statement from the CBS as a proof for a vendor payment was in fact the main contentious criteria.

The project management team has suggested to the Monitoring Agent that this is to be replaced with a letter of confirmation from the CBS regarding the payment/payments in question. A decision on this is yet to be formalized. Attaching TSA bank statement with

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every transaction for a vendor is impractical and its one of the challenges on non-salary recurrent cost that the project implementation is facing for the time being. Based on country financial regulation, Accountant General mentioned that TSA bank statement and reconciliation is to be released quarterly. However, PIU is going to initiate further discussion with MA and selected MDAs on non-salary recurrent costs.

On the other hand, reimbursement of Non-Salary Recurrent Cost was considered as one of the benchmarks of the IMF-SMP (Staff Monitored Program) to ensure the reforms are implemented fully. Following this, in a meeting assembled by the MA, WB and the FGS to discuss this issue was agreed the following:

- Review the current eligibility criteria and operating manual and update include to existing contracts, procurement thresholds (above 2001 for shopping);
- MA and core group to review payments before they are submitted to the AG to ensure criteria is met;
- Identify 12 MDAs with high spending value to fast track the implementation of this sub-component;
- Develop a strategy to help those MDAs to access to NSRC;
- Adopt shared responsibility between the Bank and the FGS to move fast tracking implementation process;
- World Bank to provide advance (notionally \$1 million to begin with) to address the first payment and act as incentive to prioritize operating costs.

However, on April 9th 2016, office of Accountant General and PIU held one-day training for MDAs director generals and other staff members from various government institutions. Over 75 participants have attended one-day training. It was a successful session that participant inter actively discussed on how non-salary recurrent cost bottle necks is solved. At opening of the training, handouts of eligibility criteria and procurement best practice written in Somali have been circulated and distributed to all participants. Following points have been discussed in detail by trainees and PIU team.

Eligibility criteria for non-salary recurrent costs to be claimed under RCRF II

Sources for NSRC:

- Section V Somalia RCRF II Project Implementation Manual
- Ministerial Order authorizing the AG not process NSRC payments unless MDAs fully adhere the eligibility criteria;
- Ministerial order:
 - Guidelines for the implementation of the web-based version of the Somalia Financial Management Information System – SFMIS

List of criteria for all costs claimed

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- Expenditures relate to goods or services;
- Expenditures are charged to the appropriate budget line of the FGS budget of one of the pilot MDAs' where MoF, Office of the Accountant General, Office of the Auditor General, National Civil Service Committee have been chosen as pilot participants.
- Expenditures are non-military;
- Expenditures incurred after effectiveness (likely signing date) of the RCRF II Grant Agreement;
- Vendor is registered in SFMIS with a Business Registration Number issued by the Ministry of Commerce and Industry; or Benadir Region, a bank account, a physical address, a working mobile phone number and a working e-mail address;
- Budget warrant duly signed by the Spending Authority as defined in the Appropriation Act;
- Budget warrant in SFMIS duly authorized by the Budget Director of MoF, the Accountant General and the Auditor General, before the Expenditure Warrant is authorized;
- Expense Voucher duly signed by the Spending Authority as defined in the Appropriation Act;
- Expense Voucher in SFMIS duly authorized by the Accountant General;
- Payment Instruction, printed directly from SFMIS, is signed by the Accountant General;
- Original of the Payment Instruction is sent to CBS;
- Vendors shall not be on the List of Individuals and Entities subject to measures imposed by paragraph 1, 3 and 7 of Security Council Resolution 1844 (2008) pursuant to Resolutions 751 (1992) and 197 (2009) concerning Somalia and Eritrea reaffirmed by UN Resolution 2142 (2014);

For cost claimed over USD 2,001, though under USD 50,000

- FGS has asked at minimum three bidders to prepare and submit a quotation;
- Bidders are requested to submit within stipulated time-lines with a minimum response time of 5 days;
- Bid evaluation shall comprise reputation & good record, financial & institutional capacity, experience, provision of equal opportunity to all eligible suppliers;
- Qualification and evaluation criteria will not be tailored to certain makes or brands, but be based on generic usage characteristics or fit-to-purpose criteria;
- No procurement activity can be broken down into smaller contracts to keep it beneath an established threshold.
- Training participants have fully understood at overall topics under discussion.

Nevertheless, there is quite significant improvement on this issue as of the third quarter of 2016. The level of understanding of the MDAs for the eligibility criteria got improved drastically due to our continuous engagement with the 12 pilot MDAs intended to go

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through the process in place. Most of those 12 MDAs have had submitted eligible documentation worth of USD 114,000 that also went through the required payment process including the MA clearance. Subsequently and as agreed, AG paid this directly to vendor accounts.

However, the World Bank declined to approve the reimbursement of the said amount, due to the fact that four contracts with the value of over USD 50,000 each, were among the submissions for reimbursement. The Bank questioned the nature and perhaps the timing of such contracts from these political institutions like the Office of the President, Office of the Parliament and Interior Ministry. As such, the Bank has turned down the entire requisition for reimbursement from the AG Office – This is despite the fact that these transactions have all met the eligibility criteria that was initially drafted by the Bank and agreed by all sides including the FGS and MA - in the first place!

Finally, in the IMF benchmark, the number of payments to achieve by December has been revised to \$450,000 from \$2,000,000 in the initial projection.

In February 2017, RCRF TTL and technical team led by the Deputy Coordinator of the project met in Mogadishu to discuss lessons learned of this item and to draft action plan for 2017. As an outcome, it has been discussed and agreed that specific object codes (like utilities, stationery, etc) have to be targeted as a way of getting NSRC disbursements moving.

Sub-Component 2.1 expanding support for recurrent cost expenditures to other regions (initially): Puntland, Jubbaland State, IGA and ISWA

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

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

Payment to existing Regional States in first quarter of 2016 totalled \$164,127.58. On the basis of Statements of expenditure submitted by States to project, \$111,822.32 has been sent over to Puntland State of Somalia where JSS has received \$52,305.26 as of March 31, 2016. In overall payment to Regional States, project has contributed \$415,367.58 of

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grant funds to those states as from the inception date of July 2, 2015 to March 31, 2016. In this quarter (Q2 of 2016) Puntland received \$116,487.03 where Jubbaland State of Somalia got \$158,839.99 which brings total transfer to region into \$275,327.02, thus total transfer to regions from the inception to June 30, 2016 is \$690,694.60. Quarter starts from July 1 to Sept 30, 2016 Puntland and JSS received \$92,454.23 and 115,284.22 respectively. As of September 30, 2016, Puntland State received total transfer of \$472,573.58 where JSS got in the total of \$425,823.47. However, JSS and Puntland had received \$274,150.73 and \$412,215.16 respectively in quarter 4 of 2016 that brought total payment to regions into \$1,584,762.94 as of Dec 31, 2016. In quarter 1 of 2017, Puntland and Jubbaland have received \$189,851.82 and \$119,084.12 respectively. Total payment given to Puntland and JSS from the inception to March 31, 2017 is \$1,893,698.88.

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

However, turning in of regional SOEs has little bit went up in quarter II of 2017. Puntland, JSS, ISWA and Galmudug have received \$903,270.32, \$321,996.50, \$101,436 and \$144,700 respectively. Total payments to the regions as of June 30, 2017 is \$3,465,101.70

Sub-Component 2.2 Inter-governmental fora on transfers and information exchange

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

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

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

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

Nevertheless, the meeting delivered productive results and promised sustained and consolidated debate and discussion on the subject matter by which the high-level participants finally agreed that the next meeting would be held in one of the regional states. The Ministry of Finance of the FGS is accounted for setting up a clear date and location of that meeting.

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

Mission of knowledge transfer to regions:

In third quarter of 2015 team led by the Project Coordinator visited Puntland State from Oct 24 through Oct 30, 2015 to undertake mission of knowledge transfer. The mission secured to induce topics in reporting and preparation of financial statements. Wide spectrum of participants from the Ministries of Health, Education and Finance attended. The stated objective of the mission was to brainstorming EAFS team in Puntland as well as recognizing a landmark of direct engagement between the FGS and the periphery entities. Mission has been successfully accomplished.

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In first quarter of this fiscal year, team comprised of eleven team members from the Ministry of Finance of the Federal Government of Somalia led by deputy PFM Coordinator and RCRFII Project Manager undertook a mission of knowledge transfer to Southwest State of Somalia with reference to an enhancement of Public Financial Management, from February 18th to 24th 2016 in Baidoa, Somalia. This mission was implemented following on the commitment made between the FGS and ministers of finance from regional governments in November 2015. The Interim South-West Administration (ISWA) was the first to respond and request for the first official team to be dispatched from the FGS's ministry of Finance in a bid to provide knowledge transfer to the regions. The Minister for Finance in ISWA, Mr. Hassan Ibrahim expressed his delight at being present during the opening ceremony of the mission of knowledge building and reiterated that such missions were far more significant than the politically oriented ones. There were several dignitaries at the event including the mayor of Baidoa.

Agenda discussions included:

1. Ways and methods of tax collections;
2. Process of budget preparation;
3. Budget execution and payment process
4. An overview of financial regulations;
5. Treasury management and expenditure

Readout of the mission and recommendations adopted thereafter is covered under the mission report that was shared with the World Bank TTL and the Project Coordinator.

Intergovernmental Fiscal Relations workshop:

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

In order to institute and operationalize the work of the technical committee, the Ministry of Finance through the support of the World Bank's Recurrent and Reform Financing (RCRF) Project, had held a workshop from 15 to 21 July, 2016, in Nairobi, Kenya. The workshop participants included members of the Ministries of Finance of the Federal Government of Somalia, Puntland State, and Jubbaland State of Somalia (JSS), Interim Southwest Administration (ISWA), and the Interim Galmudug Administration to ensure that all states had an opportunity to address their views with respect to fiscal federalism.

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The workshop was also facilitated by Somali speaking experts who have had shared intergovernmental fiscal relation theory and international practices. The presentation was very helpful to the participants to have well-informed discussions on challenges and issues that impeded the deepening of intergovernmental fiscal relations in Somalia.

The outcome of the workshop was a production of a draft Terms of Reference for a Proposed Intergovernmental Fiscal Federalism Committee (IGFFC) and this draft document entitled Considerations on Intergovernmental Fiscal Relations for the Finance Ministers Fiscal Forum (FMFF). Further, the workshop helped to produce policy suggestions to FMFF with regard to harmonizing customs tariffs in Somalia. Within this, participants hinted that customs on Khat could be a symbolic gesture to start with the harmonization exercise. (Full report of the workshop is available on separate document).

As a follow up to the above meeting and to move on what has been agreed, participants from regional entities, FGS and World Bank representatives met in Nairobi between 12 to 15th of February 2017 to discuss ways of customs harmonization and to set up the structure of the intergovernmental technical committee. The committee then elected Mr. Mohamed Kamil Yussuf, Permanent Secretary of Jubbaland Ministry of Finance, as Deputy Coordinator and five coordinating group members (one from each state). The committee agreed in their last meeting that the Coordinator would be nominated by the Federal Minister of Finance who promptly nominated Mr. Jafer Ahmed, the DG of Revenue. The work of the coordinating committee is defined in the committee TOR approved by the Finance Ministers Forum. In short, the coordinating committee members will be the focal point communication to linking all committee members.

Recommendations provided by the IGFFC

- (a) Adopt of uniform specific tax of \$2.50 on Khat. This means states that currently don't impose tax on imported Khat will introduce this specific tax and the FGS will raise its specific tax from \$2 to \$2.5. However, the FGS will introduce further surcharge to meet the IMF recommended \$3 tax per bundle.
- b) A uniform rate will be applied to all brands of Khat regardless of differences in quality and the market prices.
- c) States will also explore ways to impose surcharge on top of this specific tax (as Puntland and FGS do) and share these revenues with the districts where ports of entry are located.
- d) Licensing of Khat Importers – ISWA, JSS and IGA to license Khat importers as the FGS and Puntland currently do. This will allow emerging states to encourage importers to use official borders crossing points instead of Al-Shabaab controlled areas. The Federal Government is encouraged to enter into an agreement with Kenyan government to ensure that only valid license holders are allowed to export Khat from Kenya to Somalia.

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e) States complained that Khat importers take the proceeds of their sale in cash. Usually, when a plane delivers Khat it also takes back bags full of cash of US dollars. Committee members felt that this is putting pressure on their currency market by lowering the amount of US dollars in circulation. The committee recognizes this is the work of the Central Bank of Somalia and recommends that Ministers of Finance encourage the CBS to develop strategies to deal, regulate and mitigate this problem.

f) Only Puntland imposes international tariffs on goods coming from other parts of Somalia (Galmudug and Somaliland). To protect the Somalia's fragile common economic space states are encouraged not create inter-state trade barriers.

On June 12 and 13th, Finance Ministers Fiscal Forum meeting attended by the regional finance ministers, (Except JSS Finance Minister), Parliamentary Finance Committee chair and Governor of the Central Bank of Somalia opened in Mogadishu to discuss intergovernmental fiscal issues and to endorse recommendations put forward by the technical intergovernmental committee.

The following action points were agreed as an outcome of the meeting:

- 1) Principally agreed recommendations put forward by the technical committee on tax harmonization;
- 2) Draft National Customs Law;
- 3) Adopt Common ICT and Common goods classification to preserve national interest of the county;
- 4) Adopt a National Customs Law lead by the FGS in consultation with the FMS (Technical committee to coordinate the drafting process);
- 5) Affirmed the continuation of the consultation and reiterated that coordinated effort must be strengthened;
- 6) Recommendations to harmonize PFM act;
- 7) Recommendations that active donor funded projects are to be on-budgeted;
- 8) Affirmed the continuation of the intergovernmental fiscal dialogue for the progress and prosperity of the Somalia people;

Component 3. Support of recurrent costs in health and education sectors in FGS and eligible member states, interim and emerging administration

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

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Ministry of Finance has initiated engagement on health and education with Ministries of Health and Education in federal level to find accurate information on how to find easy way of service deliverances to the public. Many of Non - Governmental Organization and other donors are operating in Education and Health sectors. Main challenge is how to get accurate personnel data for teachers and health workers. Dialogue and consultations among concerned ministries on data collection is ongoing and will be finalized soon in order to kick off service deliverances.

Following the various discussions between the leadership of the MoF and MoH on one side and numerous engagement by the project office on the side, a TOR were draft by the project coordination office on the health sub-sector assessment and this was also reviewed and validated by the leadership of the Ministry of Health, followed by submission of a letter to the WB requesting for a TA to carry out this initial assessment.

Also, a workshop on education sector assessment was held in Nairobi in May 2016 between the Ministry of Finance and the Ministry Education with the presence of World Bank. Regional counterparts were also in attendance. The aim of the workshop was to assess financial standpoint of the sector. The Ministry of Education presented documentation explaining existing practice for financing teachers by other donors. The Ministry of Education further reported that the Government didn't pay teachers' salaries since April 2014, which the Ministry of Finance concurred too.

Consequently, it was agreed that RCRF-II Project to support financing salaries and allowance of teachers both in FGS level and Regional Level but subject providing qualifying numbers of teachers that are appropriately reflected in the FGS supplementary 2016 budget. As of this, documentation of 1,258 teachers has been preliminary reviewed by the Bank in FGS level and 1,195 teachers in Puntland.

However, an inter-ministerial meeting to move forward this component was held between the Ministry of Finance and the Ministry of Education, Culture and Higher Education in October at the Ministry of Finance. In this meeting it was agreed that those teaching purely at Public Schools would only be eligible at this time to receive payment, but subject through certification process. Subsequently, the Ministry of ECHE provided 1083 teachers as currently teaching at Public Schools across ten regions namely Banadir, Lower Shabelle, Middle Shabelle, Bay, Bakool, Hiran, Mudug, Gedo, Lower Jubba and Galgaduud.

On 19th March 2017, a discussion between the government and the Bank on key mandatory fields on teachers payroll on specific information that is required to be completed in order to fast track the implementation of the teacher salaries was held at Chelsea Village in Mogadishu. As going forward and as to fast track this issue, we have agreed to phase out financing teachers salaries starting from Banadir area. The total number of teachers to be supported under RCRF II in Banadir region will not exceed

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three hundred and eight (319) in 2017 as presented by the Ministry of Education. Numbers of teachers in the regions are being submitted by the respective administrations.

In this reporting period, the Ministry of Education, Culture and Higher Education of FGS submitted all necessary documents relate to teachers' financing and now pending review with the World Bank.

Component 4: Project Management and Coordination:

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

Payroll Training

The Ministry of Finance through PFM Reform Coordination Unit (PFMRCU), organized one-day induction training for Ministries, Departments and Agencies (MDAs) of the Federal Government of Somalia (FGS). In its effort to reform payment transactions, the Ministry of Finance, with assistance from World Bank Group, recently undertook a rigorous civil servants payroll exercise for all MDAs of the FGS. MDAs Finance Directors, Accountant Heads, HR Directors attended the training session. The training which took place at Villa Hargeisa, Parliament building in Somalia was facilitated by the Deputy PFM Coordinator and EAFS heads in the Ministry of Finance who extensively shared their experiences and made detailed presentations about errors observed in the payroll systems submitted by various Ministries, Departments and Agencies of the FGS.

The session embraced a highly participatory methodology, with numerous practical examples and experiences, which was effective in passing on knowledge to the participants. To further beef up their understanding of the payroll system, the participants had an opportunity to actively interact with the facilitators. It was observed that the participants were highly engaged throughout the training, very eager to learn and ready to report back and pass on this knowledge to their junior staff. Mr. Ahmed Yusuf Mumin (Siraaji), the Accountant General of the FGS welcomed the participants, introduced the facilitators, and officially opened the training.

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In his opening remarks, Mr. Siraaji welcomed participants to the training and particularly noted that he was delighted to be in attendance to witness the commencement of yet another engagement among FGS MDAs. He noted that there is serious errors always generated by MDAs upon submission of Civil Servants Payroll whose this training objective is to strengthen the payroll systems and come over those errors identified by EAFS consultants.

The Accountant General further noted that modest improvements in Public Financial Management couldn't be realized unless and until MDAs avoid frequent mistakes in their payroll systems. He strongly encouraged them not to repeat such errors once this training sessions ends.

The Accountant General informed the participants that a comprehensive payroll system, a political good will and effective implementation of the PFM reform would be a milestone for the FGS to retain its prestigious position within the International Financial Institutions.

On behalf of the FGS, he finally thanked World Bank Group, PFMRCU and EAFS team for collectively supporting this country and for their determination to effectively reform the FGS' public financial mechanism and move this country to a well prosperous and better future. He concluded by wishing the participants a productive debate with the facilitators. At this point, he officially declared the workshop open.

Participants had different questions covered one important topic – whose responsibility keeping staff duties segregated, checking personnel files completed and at the same time liaising those updated files to the National Civil Service Commission (NCSC). It seemed that MDAs quietly anxious getting clear clarification about these by suggesting that Finance Officers/Directors mainly focused on developing and updating payroll system, completing monthly financial statements and preparing respective annual budgets. Thus, training was successful and attendees have been brainstormed with relevant information on respective topics.

IMPLEMENTATION STATUS:

Line Ministry of the project	The project is under the supervision of the Ministry of Finance and other Ministries, Agencies and Departments (MDAs).
Strategic goals of the project	The strategic goal of the project is to support an operational payroll and payment system for the non-security sectors of the Federal Government of Somalia, support of Non salary recurrent cost for MDAs, and strengthen services to Regions of Puntland, Jubbaland and emerging States Administrations

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Staffing	All 6 Consultants to the EAFS contract plus the PFMRCU senior admin officer. Deputy PFM Coordinator who became RCRF II project manager has been done. Two Regional Program Managers have been recruited.
Procurement plan	<p>Almost all TORs for the consultants under component has been finalized and submitted for review.</p> <p>Recruitment for the TA CBS was rejected by the WB and regional TA was contracted.</p> <p>Specification for the planned project vehicles has been prepared and procurement process underway accordingly.</p>
Regional implication	Leadership of the MoF fully appreciates the need to accommodate the regions both existing and emerging. Payment processing and transfer for the JSS and Puntland regional states has fully been tested and tried within the FGS systems.

CHALLENGES

Current eligibility criteria and difficulties in meeting certain conditions by the MDA on non-salary recurrent expenditures make utilization and reimbursement processes almost impossible. The need for a TSA statement from the CBS as a proof for a vendor payment was in fact the main contentious criteria. The project Coordinator has suggested to the Monitoring Agent that this to be replaced with a letter of confirmation from the CBS regarding the payment/payments in question. A decision on this is yet to be formalized. Attaching TSA bank statement with every transaction for a vendor is impractical and its one of the challenges on non-salary recurrent cost that the project implementation is facing for the time being. Based on country financial regulation, Accountant General mentioned that TSA bank statement and reconciliation is to be released quarterly. However, Project Management teams going to initiate further discussion with MA and World Bank on non-salary recurrent costs.

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

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KEY PROJECT INFORMATION

Project Name:	Recurrent Cost and Reform Financing Project – Phase II
Project ID:	P154875
IDA Credit/Grant No.:	TF0A0534
Implementing Agency:	Ministry of Finance and Economic Planning
Effectiveness Date:	02 July 2015
Closing Date: For this year	31 December 2017
Credit/Grant Amount:	US\$ 39 million
Program Duration for this year (2017)	12 months
Closure Period End Date:	30 June, 2020
Disbursed Amount:	US\$ 35,228,300.40

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“Reserve for Auditor General’s Opinion”

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FINANCIAL REPORT

The Period Ended June 30, 2017

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STATEMENT OF PROJECT MANAGEMENT’S RESPONSIBILITIES

The Project Management is responsible to ascertain that the progress report and financial statements of the Project for the period ended June 30, 2017 are prepared, in all material respects, in accordance with the basis of preparation and accounting policies set out in Note 3 to the financial statements. In preparing these financial statements, the Project Management is required to select suitable accounting policies and then apply them consistently in conformity with Cash Basis International Public Sector Accounting Standard (Cash Basis IPSAS) and the requirements of Financial and Accounting procedure of the State, 1961 as amended.

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

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

Signed on behalf of the Project Management:

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Ahmed Yusuf Muumin,
Accountant General

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Funding summary

The Project implementation for this year is 12 months from 01 January 2017 to 31 December 2017, with an approved budget of US\$ 39,000,000 from 2015 to 2017 and commitment of the donors is as highlighted in the table below:

Source of funds	Donor Commitment	Amount received up to June 30, 2017	Undrawn balance up to June 30, 2017
	US\$	US\$	US\$
	(A)	(B)	(A)-(B)
Somalia Multi-Partner Fund (MPF) – World Bank	39,000,000	35,228,300.40	3,771,699.60
Total	39,000,000	35,228,300.40	3,771,699.60

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NOTES TO THE FINANCIAL STATEMENTS

1. General Information

The principal address of the reporting entity is:

Ministry of Finance
Villa Somalia
Mogadishu
Somalia

2. Basis of preparation

These special purpose financial statements have been prepared in accordance with IPSAS Financial Reporting under The Cash Basis of Accounting issued by Public Sector Committee of the International Federation of Accountants (IFAC-PSC). They are presented in United States Dollar (US\$). The measurement basis used is the historical cost basis except where otherwise stated in the accounting policies below.

3. Significant Accounting Policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied during year, unless otherwise stated

(a) Reporting entity

The financial statements are for the **Recurrent Cost and Reform Financing Project – Phase II (P1154875, TF0A0534) implemented by the Federal Government of Somalia (FGS) through The Ministry of Finance**. The transactions to be captured are only those that are controlled by the reporting entity and those controlled by third parties for and on behalf of the reporting entity. For purposes of these financial statements there were no third-party transactions reported in respect of the project activities.

(b) Reporting currency and translation of foreign currencies

The functional and reporting currency is the United States Dollar (US\$), which is accepted as legal tender in the Federal Republic of Somalia. Items included in the financial statements are measured in the currency of the primary economic environment in which the entity operates.

(c) Reporting Period

The reporting period for these financial statements is covered for the period ended 30 June 2017.

(d) Payments by Third Parties

During the quarter ended, the project did not benefit from any goods and services as reported to have been purchased on its behalf as a result of cash payments made by third parties during the year.

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NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(e) Receipts

Receipts represent cash received by the Recurrent Cost and Reform Financing Project – Phase II (P1154875, TF0A0534) during the period and comprise external assistance from cash disbursements received under Somalia Multi-Partner Fund. The cash disbursements have been recognized as revenue and includes in the financial statements when payments are made from the project Designated Accounts (DA) A and (DA) B which were operated as a holding accounts to the main Treasury Single Account (TSA) and direct payments made by WB on behalf of FGS. The closing balance on the Designated Accounts was also included as revenue receipts from the World Bank.

(f) Expenses

Expenditure represents outlays of cash made by the project or other agencies for and on behalf of the project. The expenses comprise both of recurrent and capital expenditure and in general they are included in the financial statements when cash is paid out.

(g) Capital items/Non-current assets

As of June 30, 2017, there are Capital items purchased at project money. Under the government's cash basis of accounting, capital items have been fully expensed in the year of purchase. However, these assets are recorded in the Fixed Asset Registers at historical cost as a memorandum record with effect from effective date of the project.

(h) Foreign currency transactions

Foreign currency transactions denominated in foreign currencies would be converted into United States Dollars (US\$) at the exchange rate ruling on the date of the transaction; realized gains and losses resulting from these transactions would be recognized in the Statement of Receipts and Payments. Monetary assets and liabilities denominated in foreign currency at the year-end would be translated at the closing rate of exchange with the resulting exchange gains/(losses) dealt with through the Statement of Receipts and Payments. However, for purposes of this accounting policy, there was no other foreign currency transactions than US Dollar translated at the reporting date.

(i) Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise of deposits held at call with Central Bank of Somalia.

(j) Employee benefits

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Employee benefits include salaries, allowances and other related-employment costs and these have been recognized in the financial statements only when actual payments are made.

Employee salaries and allowances eligible for reimbursement under the RCRF II project are paid in cash at the Central Bank of Somalia through bank accounts employees have with licensed private banks. To enable this process, payments are made over few days for each monthly payroll. Thus, employees are then collecting their salaries from their bank accounts with licensed private banks.

(k) Authorization date

The financial statements were not authorized yet for publication by the Accountant General.

4. Exchange rates

All monetary amounts in the financial statements are expressed in United States Dollars (US\$). The estimated US\$ closing rates for major currencies were:

	Previous Years US\$	2017 US\$
Somali Shilling	22,500	22,500
Great Britain Pound	0.641584	0.641584
Euro	0.825748	0.825748