

AFRICAN DEVELOPMENT BANK GROUP



REQUEST TO TRANSFER RESOURCES FROM ARREARS CLEARANCE WINDOW OF FRAGILE STATES FACILITY (FSF) (PILLAR II) TO ADF

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Acronyms and Abbreviations

ACC	Advanced Commitment Capacity
ACW	Arrears Clearance Window (of FSF)
ADB	African Development Bank
ADF	African Development Fund
CSP	Country Strategy Paper
DANIDA	Danish International Development Agency
ESW	Economic and Sector Work
FFMA	Financial Management Department (of the ADB)
FSF	Fragile States Facility
HIPC	Highly Indebted Poor Countries (initiative)
IN	Information Note
MDRI	Multilateral Debt Relief Initiative
OECD	Organization for Economic Cooperation and Development
OpsCom	Operations Committee (of the ADB)
OSFU	Fragile States Unit (of African Development Bank)
PBA	Performance-Based Allocation System
PCC	Post Conflict Countries
PCCF	Post-Conflict Countries Facility
PCNA	Post-Conflict Needs Assessment
RD	Regional Department
RMC	Regional member Country
SD	Sector Department
SSW	Supplemental Support Window (of FSF)
TA	Technical Assistance
TCB	Technical Assistance and Capacity Building
TSW	Targeted Support Window (of FSF)
UA	Unit of Account

Executive Summary

1. The Arrears Clearance Window (Pillar II) of the Fragile States Facility (FSF) has a balance in the amount of UA 52.88 million as at end July 2010, of which UA 3.19 million from the ADF and UA 49.69 million from the ADB. Under the ADF-11 cycle (2008-2010) Pillar II resources were provided by both the ADB and the ADF to assist in clearing arrears and servicing any maturities of selected countries until they qualify for debt relief under the HIPC initiative. Whereas Togo and Cote d'Ivoire qualified for arrears clearance during the ADF-11 cycle, three countries (Somalia, Sudan and Zimbabwe) could not qualify at the time. As such, they are currently under sanctions with the Bank due to the arrears.

2. The amount needed to clear the arrears for Somalia, Sudan and Zimbabwe is estimated at UA 561 million as at July 2010, and far exceeds the resources currently available in Pillar II of the FSF, or those likely to be provided in the ADF-12 cycle. Among the three countries, Zimbabwe, the most likely country to qualify for arrears clearance in ADF-12 (2011 – 2013), has arrears amounting to UA 333.453 million as at end July 2010. In accordance with Bank policy, ADF cannot clear its own arrears, neither can ADB. Thus, the UA 326.558 million of Zimbabwe's ADB arrears will need to be cleared using ADF resources, while the UA 6.894 million of ADF arrears will be cleared using ADB resources. Most of the unused balance of UA 52.88 million in Pillar II can neither be used for the bulk of Zimbabwe's arrears since they are mostly ADB resources, nor can these resources be transferred to any other pillar of the FSF given the segregated nature of the three FSF pillars. It would therefore mean that a substantial part of the UA 52.88 million in FSF Pillar II could remain unutilized up to end 2013 if no action is taken.

3. Management proposes to transfer UA 49.69 million of the resources of ADB origin from FSF Pillar II to boost the ADF-12 Advanced Commitment Capacity (ACC). The UA 3.19 million of ADF resources remaining in Pillar II would be available for clearance of ADB arrears during the ADF-12 period. In the ADF-12 replenishment discussions, Management has committed to submit to the ADF Deputies a Report regarding the utilization of the FSF-Pillar II resources by the Mid Term Review of ADF-12.

4. Management seeks the authorization of the Boards of Directors to write to the Boards of Governors to request the transfer of unutilized resources of UA 49.69 million in FSF-Pillar II. The transfer is intended to boost the ACC of the ADF-12 replenishment. This proposal is made as part of the maximum efforts on the part of Management to improve the level of internally generated resources for the ADF-12, and also to ensure efficiency in the utilization of idle operational resources held within the Bank. By releasing these resources, Management commits to undertake appropriate resource mobilization efforts to clear the arrears of Sudan and Somalia when their socio-economic and political situation improves to the point where they qualify for assistance from the FSF-Pillar II operations.

5. The Boards of Directors are invited to consider and approve the proposals made in this paper regarding the use of the FSF-Pillar II resources in the amount of UA 49.69 million.

1. Introduction

1.1 The Arrears Clearance Window (Pillar II) of the Fragile States Facility (FSF) had a balance of UA 52.88 million as at July 2010. This balance remained after all the targeted arrears of Côte d'Ivoire and Togo were cleared, allowing them to qualify for debt cancellation under the HIPC initiative early in the ADF-11 cycle (2008-2010). The resources were provided by both the ADB and the ADF to assist in clearing arrears and servicing any maturities of selected countries until they effectively qualified for debt relief under HIPC initiatives. Whereas Togo and Cote d'Ivoire qualified for arrears clearance under ADF-11, three countries (Somalia, Sudan and Zimbabwe) still have protracted arrears towards the Bank Group.

1.2 This document proposes that the Board of Directors approve Management's request for authorization from the Board of Governors to transfer unutilized resources in the amount of UA 49.69 million from Pillar II of the Fragile States Facility (FSF) as presented in Table 1 below. These funds would contribute to boost the Advanced Commitment Capacity (ACC) of the ADF 12 Replenishment, while the balance of UA 3.19 million (being resources of ADF origin) would be used to support arrears clearance under the ADF-12 cycle (2011-2013). The proposal is made as part of the maximum efforts on the part of Management to mobilize internally generated resources to support the ADF replenishment. It is also consistent with the rules and regulations governing the disposition of unused FSF resources. The transfer of the UA 49.69 million (being resources of ADB origin) requires the approval of the Board of Governors.

Table 1: Summary of Utilization of FSF-Pillar II Balance

	<i>(in UA million)</i>		
	<i>ADB</i>	<i>ADF</i>	<i>TOTAL</i>
<i>Balance of Resources</i>	<i>49.69</i>	<i>3.19</i>	<i>52.88</i>
<u><i>Proposed use in ADF-12</i></u>			
<i>Arrears Clearance</i>	<i>0.00</i>	<i>3.19</i>	<i>3.19</i>
<i>Boost the ACC of ADF - 12</i>	<i>49.69</i>	<i>-</i>	<i>49.69</i>

2. Availability and Use of FSF-Pillar II Resources in ADF 12

2.1 During the ADF-11 replenishment the Arrears Clearance Window or Pillar II of the FSF was allocated resources in the amount of UA 129.10 million. The ADF-11 allocations were augmented with carry-over resources from the ADB and ADF windows of the Post-Conflict Country Facility (PCCF). These amounted to UA 165.64 million, with the cumulative income earned on PCCF resources in the amount of UA 13.72 million, thus bringing the total resources in the Arrears Clearance Window (Pillar II) of the FSF to UA 308.46 million. Part of this amount was utilized in clearing the arrears of the Republic of Cote d'Ivoire in the amount of UA 240.96 million and the arrears of Togo in the amount of UA 14.62 million.

2.2 Only Togo and Cote d'Ivoire were programmed for arrears clearance in the ADF-11 cycle. By April 2009, the two operations had been successfully implemented, in line with the recommendations of the Deputies during the ADF-11 replenishment. Total resources used for the two operations amounted to UA 255.58 million, thus leaving a residual balance of UA 52.88 million, of which UA 3.19 million is from the ADF and UA 49.69 million from the ADB allocation to FSF-Pillar II under ADF-11. Table 2 (below) provides a detailed account of Pillar II resource utilization.

Table 2: Utilization of Pillar II Resources (UA million)

	ADF	ADB	TOTAL
Carry-over PCCF	102.94	62.70	165.64
Allocation ADF 11	129.10	-	129.10
Income (cumulative December 2008)	3.80	9.92	13.72
Total resources	235.84	72.62	308.46
Disbursement 2008 (Togo)	0.05	14.57	14.62
Disbursement 2009 (Côte d'Ivoire)	232.60	8.36	240.96
Total disbursements	232.65	22.93	255.58
Balance as at July 2010	3.19	49.69	52.88

Source: OSFU

2.3 Three remaining countries, Zimbabwe, Sudan and Somalia, continue to experience serious external debt problems and still carry protracted arrears towards the Bank Group. Management has consulted with the ADF Deputies regarding the arrears clearance of these countries in the context of the ADF-12 Replenishment. Current assessments are that Zimbabwe is the most likely to qualify for arrears clearance in the ADF-12 cycle (2011 – 2013). The estimated total resources required to clear the arrears of the three countries amount to UA 561 million, as at July 2010, and exceed by a wide margin the projected allocations for the FSF-Pillar II from the ADF-12 (see Table 3). As presented during the second Replenishment meeting (Cape Town, February 2010), the probability of implementing arrears clearance operations during the ADF-12 cycle has been assessed as high for Zimbabwe, medium for Sudan and low for Somalia.

Table 3: Arrears Clearance Requirement for Somalia, Sudan and Zimbabwe (in UA '000)

Country	ADB	ADF	Total	Probability of implementing an arrears clearance plan in ADF-12
Somalia	13,206.89	40,084.33	53,291.22	Low
Sudan	106,750.97	67,396.61	174,147.58	Medium
Zimbabwe	326,558.43	6,894.36	333,452.79	High
Totals	446,516.29	114,375.30	560,891.59	

2.4 At the third replenishment meeting in Abidjan (May 2010), Management proposed to allocate UA 404 million of ADF-12 resources to Pillar II, for the clearance of arrears to the ADB during the ADF-12 period. In response to Deputies' guidance who considered this amount too high, Management subsequently revised its proposal to UA 359 million.

3. Justification for the Transfer of Unused FSF-Pillar II Resources

3.1 The Board of Directors recalls that the FSF is a financing vehicle with three complementary pillars that have segregated grant resources. Under Pillar I, the Supplemental Support Window, a list of nine (9) countries approved by Deputies have set allocations for the ADF-11 replenishment period. Management is assessing the eligibility of these countries for the second cycle of support under ADF-12 with a view to revising the list of Pillar I

beneficiaries to include new entrants and those likely to be phased-out. As was the case in ADF-11, resources under this pillar will be provided through the ADF-12 replenishment. FSF Pillar I allocations under ADF-11 had been fully committed as at end June 2010.

3.2 Regarding Pillar II operations, in ADF-11 Deputies allowed for Togo and Cote d'Ivoire to benefit from the arrears clearance under the FSF. (para 2.2 above). In 2008 the arrears for Togo were cleared, while those of Côte d'Ivoire were cleared in 2009. A significant portion of the FSF-Pillar II balance (UA 52.88 million) obtained from the timely arrears clearance exercise is expected to remain unutilized during ADF-12 cycle given the Bank's arrears clearance policy whereby ADB clears ADF arrears and vice versa, and the segregated structure of the FSF pillars.

3.3 Zimbabwe, the most likely country to qualify for arrears clearance in ADF-12, had arrears amounting to UA 333.45 million as at end July 2010. These arrears comprise UA 326.55 million from the ADB that will have to be cleared using ADF resources, and UA 6.89 million from the ADF that should be cleared by the ADB. The arrears are expected to increase to UA 359.39 million for the ADB and UA 8.54 million for the ADF by ADF-12 Mid-Term Review. The majority of the unused Pillar II balance of UA 52.88 million can neither be used for the bulk of Zimbabwe's arrears being mostly ADB resources, nor be transferred to any other pillar of the FSF given the segregated nature of its three pillars. Given the lower probability of Sudan and Somalia requiring these funds, they could remain unutilized up to end 2013.

3.4 In this regard, to ensure efficiency in the utilization of idle operational resources held within the Bank and with a view to maximize internally generated resources management proposes to transfer the unutilized resources of UA 49.69 million to boost the Advanced Commitment Capacity (ACC) of the ADF-12 replenishment.

4. Conclusion and Recommendations

4.1 Conclusion: Zimbabwe is the most likely country to benefit from the FSF-Pillar II operations in ADF-12. At end July 2010, the country had arrears in the amount of UA 326.558 million from the ADB and UA 6.894 million from the ADF. These arrears are expected to increase to UA 359.396 million for the ADB and UA 8.543 million for the ADF by ADF-12 Mid-Term Review in 2012. Should the country become eligible, ADB arrears could be cleared by

the expected ADF-12 allocations to FSF-Pillar II, while ADF arrears could be cleared by additional resource mobilization efforts. A residual of UA 49.69 million would remain idle in the FSF-Pillar II during the next three years if no action is taken.

4.2 Recommendations: Management therefore seeks the authorization of the Boards of Directors to request the Boards of Governors to approve the transfer of unutilized FSF-Pillar II resources of ADB origin in the amount of UA 49.69 million to boost the Advanced Commitment Capacity (ACC) of the ADF-12.

4.3 This proposal is made as part of the maximum efforts by management to improve the level of internally generated resources for the ADF-12, and also to avoid idle resources being held within the Bank. Management will undertake appropriate resource mobilization efforts to clear the arrears of Sudan and Somalia when their socio-economic and political situations improve to the point where they qualify for assistance from the FSF-Pillar II.

4.4 Further, Management will prepare a Report regarding the FSF-Pillar II resource utilization for the ADF-12 Mid-Term Review.

4.5 The Boards of Directors are invited to consider and approve the proposals made in this paper regarding the use of the FSF-Pillar II resources in the amount of UA 49.69 million.

**PROPOSAL FOR TRANSFER OF RESOURCES FROM THE ARREARS CLEARANCE
WINDOW OF THE FRAGILE STATES FACILITY (FSF PILLAR II) TO ADF**

CORRIGENDUM

1. **Executive Summary, paragraph 2, penultimate sentence should read** *“Most of the unused balance of UA 52.88 million in Pillar II derived from ADB cannot be used for the bulk of Zimbabwe’s arrears which are owed to the ADB nor can these resources be transferred to any other pillar of the FSF given the segregated nature of the three FSF pillars without prior approval of the ADB Board of Governors”.*
2. **Paragraph 4, first line should read** *“Board of Directors to write to Board of Governors”.*
3. **Paragraph 5, should read:** *“The Board of Directors is invited to consider, for further transmission to the Board of Governors, the proposals made in this paper regarding the use of FSF – Pillar II resources in the amount of UA 49.69 million.”*
4. **Main Document, paragraph 1.2, last sentence should read** *“The UA 49.69 million being net income allocations of the Board of Governors for a specific purpose, the proposed change in the use of these allocations requires the approval of the Board of Governors”.*
5. **Paragraph 3.3, second to last sentence should read** *“The majority of the unused Pillar II balance of UA 52.88 million derived from ADB cannot be used for the bulk of Zimbabwe’s arrears which are owed to the ADB”.*
6. **Conclusion, Paragraph 4.5, the sentence should read** *“The Board of Directors is invited to consider, for further transmission to the Board of Governors, the proposals made in this paper regarding the use of FSF – Pillar II resources in the amount of UA 49.69 million.”*