

**SPECIAL REPORT No 10/2003****concerning the effectiveness of the Commission's management of development assistance to India  
in targeting the poor and ensuring sustainable benefits, together with the Commission's replies***(pursuant to Article 248(4), second subparagraph, EC)**(2003/C 211/02)***CONTENTS**

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**GLOSSARY OF ACRONYMS**

ALA	Asia-Latin America
BAIF	Bharatiya Agro Industries Foundation
DPEP	District Primary Education Programme
EC	European Community
GNP	Gross National Product
KHDP	Kerala Horticulture Development Project
KMP	Kerala Minor Irrigation Project
NGO	Non-governmental organisation
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
PESLE	Programme for the enrichment of school level education

## SUMMARY

I. Cooperation between the European Community and the Republic of India goes back at least 30 years and is presently governed by the Cooperation Agreement of 1994. Some 70 % (or 481 million euro) of the EC's financial assistance disbursed over the period 1990 to 2001 was provided for development cooperation activities (the remainder covering a number of other areas including food aid and humanitarian aid). These activities included a large number of agricultural and rural development projects, as well as two sector-support programmes for education and health (see paragraphs 1 to 7).

II. The Court has examined eight of these projects and programmes, in particular to see how they are targeting the poorer sections of the population, what chances there are that the benefits will be sustained beyond the end of the EC-financed activity, and what kind of donor coordination activities take place (see paragraphs 8 to 10).

III. The Court concludes that the Commission's management has been reasonably successful in targeting the poor and in addressing sustainability for the majority of the eight projects/programmes audited in India. More systematic attention for these issues throughout the whole project/programme life cycle could, however, have improved the results (see paragraphs 11 to 37).

IV. A sector-wide approach can offer certain advantages over a project-based approach. These include more closely harmonised, coherent policies and strategies, wider impact and better chances of sustainability. Such an approach also requires that donors have sufficient confidence in the capacity of the beneficiary's administration to manage sector-wide programmes and to account for their implementation, results and costs. However, up to now there has not been a true sector-wide approach in the Indian education and health sector programmes. Only the EC has so far been prepared to support a sector-programme approach in India, while other donors operate through a project-based approach. As a result, it has not been possible to establish common accountability and reporting systems in these nationwide programmes. For the above reasons, opportunities to create synergy and efficiency through a truly coordinated sector-wide approach have not materialised. Whereas inter-donor coordination in the education sector programme has resulted in a well-appreciated system of joint review missions, for the health sector, more informal channels for coordination were used (see paragraphs 38 to 44).

V. The EC's new country strategy for cooperation with India does not fully apply the approach outlined in the Commission's recent communication on fighting rural poverty, as it limits EC intervention to the health and education sectors, leaving aside other key sectors (agriculture, natural resources management) identified in that communication as needing to be addressed if rural poverty is to be tackled successfully (see paragraphs 45 to 47).

VI. The following recommendations are made on the basis of the Court's observations and conclusions:

- 'targeting the poor' as well as 'sustainability' should be given more systematic attention throughout the life of a project/programme (see paragraphs 53 and 56),
- chances of sustainability would improve if projects/programmes were allowed an appropriate implementation period from the outset, in combination with regular reviews, and included a proper exit strategy (see paragraph 56),

- when considering contributing to a sector programme through budget support, the Commission (together with other donors) should ensure both beforehand and — later — in the course of implementation, that the direction on public finance (including reporting, accounting and auditing systems) taken by the country concerned is satisfactory. In a situation where capacity-building is unlikely to ensure adequate accountability for unearmarked budget support, the Commission should consider other forms of support (see paragraph 59),
- in the light of its overall poverty reduction objective, the Commission could make its new EC-India country strategy more comprehensive by addressing important issues like agriculture and natural resources management (see paragraph 61).

## INTRODUCTION

### Background

1. The basic legal framework for the EC cooperation with India currently in force is the 'ALA Regulation' of 1992 <sup>(1)</sup> which describes the aims of the Community's development and cooperation policies and the main areas of assistance. Article 4 of the Regulation states that 'financial and technical assistance shall be targeted primarily on the poorest sections of the population ...'

2. More specifically, cooperation with India is governed by the Cooperation Agreement on Partnership and Development, which entered into force in August 1994 <sup>(2)</sup>, replacing the earlier cooperation agreements of 1973 and 1981. According to Article 16 of this agreement, which deals in particular with development cooperation, projects and programmes are to be targeted on the poorer sections of the population. Particular attention is to be given to rural development with participation of the groups to be targeted and, where appropriate, the involvement of qualified non-governmental organisations. Cooperation is to pursue project and programme efficiency, sustainability and respect for the environment.

3. Following the signing of the Cooperation Agreement, an EC-India cooperation strategy to the year 2000 was agreed in December 1994. This document sets out general strategies for development as well as for economic cooperation. It states that the EC's support for development in India should have a strong

impact on the alleviation of poverty, which is considered one of the most critical issues. It also indicates that the EC's cooperation programme will support the implementation of appropriate sector policies as well as development projects.

4. A new strategy paper for the period 2002 to 2006 was being prepared at the time of the audit and was formally approved by the Commission in August 2002 <sup>(3)</sup>. The paper defines the elimination of poverty as the overall guiding principle governing EC cooperation activities in India. The Commission will continue its cooperation with the Central Government through the sectoral support programmes in elementary education and health and family welfare. In addition it plans to develop a special partnership with one Indian State and to spend available resources mainly in that State, with elementary education and basic health as the core areas.

### Budgetary significance

5. Total disbursements on all cooperation activities during the 12-year period 1990 to 2001 amounted to 657 million euro, an annual average of about 55 million euro. This includes disbursements under all relevant budget lines, including development and economic cooperation, humanitarian and food aid, non-governmental organisations (NGOs) programmes, and several other, minor, programmes. As can be seen in *Table 1*, over 70 % of total disbursements was spent on development cooperation.

<sup>(1)</sup> Council Regulation (EEC) No 443/92 of 25 February 1992 on financial and technical assistance to and economic cooperation with the developing countries in Asia and Latin America (OJ L 52, 27.2.1992).

<sup>(2)</sup> OJ L 223, 27.8.1994.

<sup>(3)</sup> Written procedure E/1642/2002 (COM(2002) 3117 of 14 August 2002).

Table 1

**Disbursements on cooperation activities in India, 1990 to 2001**

(in million euro)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	Total
Total disbursements, all relevant budget headings	43	30	45	29	48	47	81	82	45	73	50	84	<b>657</b>
of which on:													
Development cooperation	34	13	21	14	37	37	73	71	35	60	31	55	<b>481</b>
Economic cooperation	2	5	2	3	4	4	1	2	1	2	3	3	<b>32</b>
Humanitarian and food aid	2	8	18	8	3	1	0	2	1	1	8	16	<b>68</b>
Cofinancing with NGOs	4	3	4	4	4	4	5	5	6	8	6	7	<b>60</b>
Other budget headings	1	1	—	—	—	1	2	2	2	2	2	3	<b>16</b>

Source: Data provided by EuropeAid.

6. Disbursements on development cooperation totalled 481 million euro over the same period, an average of 40 million euro per year. From the detailed data in *Table 1* it can be seen that the level of disbursements on development cooperation activities increased significantly over the six-year period 1996 to 2001 (annual average of 54 million euro), compared to the preceding six-year period (annual average of 26 million euro). This change is directly related to the introduction of the sector-support programmes for education (in 1994) <sup>(1)</sup> and health (in 1998) <sup>(2)</sup>. The EC is an important grant donor to India. Nevertheless, its aid is modest in relation to the overall Official Development Assistance (ODA) received by India (which amounted to approximately 1 500 million US dollars per year including soft loans during the period 1997 to 1999) and in relation to the amounts invested by India itself. ODA as a percentage of India's GNP amounted to only 0,3 % over the same period <sup>(3)</sup>.

**Development cooperation programme**

7. The 2001 portfolio of the Commission's development cooperation activities under implementation in India can be subdivided into three broad types of activities:

- 12 agricultural and rural development projects implemented by government agencies,
- two sector-support programmes, one for education, which is to come to an end in 2003 (but is to be followed by a new programme), and one for health and family welfare,
- four projects, implemented by large Indian and non-Indian NGOs, three of which focus on rural development and one on education.

<sup>(1)</sup> Tranche payments of 20, 40, 40 and 40 million euro were made in 1994, 1996, 1997 and 1999, respectively.

<sup>(2)</sup> Tranche payments of 16, 7, 14 and 27 million euro were made in 1998, 1999, 2000 and 2001, respectively.

<sup>(3)</sup> OECD website: 'Recipient aid at a glance, India'.

**The Court's audit**

8. The objective of the Court's audit was to determine whether the Commission has managed the programme of development assistance to India effectively. The audit focused on the following key questions:

- has the Commission ensured that its projects/programmes target the poorer sections of the population?
- has the Commission managed its projects/programmes in a manner that ensures that they will be sustainable <sup>(4)</sup>?
- has the Commission created — together with the other main donors — effective coordination mechanisms in order to ensure that coherent approaches are followed in the sectors which are supported?

9. The audit included the examination of eight development projects/programmes covering all three types of activities, as described in paragraph 7. In view of their size, the two sector-support programmes in education and health were both included <sup>(5)</sup>. In addition, four (out of twelve) government-implemented projects were selected, as well as two (out of four) NGO-implemented projects. These eight activities represent 74 % of the total value committed (660 million euro) of the Commission's ongoing development cooperation projects/programmes in 2001 for India. The full list of projects/programmes audited is shown in *Table 2*, together with budgetary information.

<sup>(4)</sup> An activity is considered sustainable when it is able to deliver benefits to the target group for an extended period of time, after the main assistance has ended.

<sup>(5)</sup> The official titles of the two sector programmes are: Sector Programme for the Development of Primary Education and Support for Health and Family Welfare Sector Development. In the report they will be referred to as the sector programmes for education and health respectively.

Table 2

**Projects/programmes audited***(in million euro)*

Name of project/programme	Year of signature of Financing Agreement	Actual period of implementation	Commitments	Disbursements as per 1.12.2002
<b>AGRICULTURAL AND RURAL DEVELOPMENT PROJECTS BY GOVERNMENT AGENCIES</b>				
Doon Valley Integrated Watershed Management Project (Doon Valley)	1991	1992-2001	23	23
Kerala Horticulture Development Project (KHDP)	1992	1993-2002	29	26
Kerala Minor Irrigation Project (KMIP)	1992	1994-2000	12	6
Sidhmukh and Nohar Irrigation Project	1993	1994-2001	45	40
<b>NGO-IMPLEMENTED PROJECTS</b>				
Transfer of technologies for sustainable development (BAIF)	1995	1996-present	20	15
Programme for the Enrichment of School Level Education (PESLE)	1999	1999-present	11	4
<b>SECTOR-SUPPORT PROGRAMMES</b>				
Sector Programme for the Development of Primary Education (DPEP)	1993	1994-2003	150	149
Support for Health and Family Welfare sector development	1997 + 2001	1998-present	200 + 40	67
<b>Total</b>			<b>530</b>	<b>330</b>

10. Project files, both in Brussels and in the Commission's Delegation in Delhi, were examined and Commission officials were interviewed. Audit visits were carried out to all eight projects/programmes selected, during which discussions were held with Government of India and State government officials, the Comptroller and Auditor-General of India, as well as with representatives of the implementing organisations. On several occasions meetings were also held with project beneficiaries.

12. On the other hand, at the operational level four of the eight audited projects/programmes gave clear definitions identifying poor, disadvantaged people as their target group <sup>(1)</sup>. The health sector programme was less specific in its design, with its target group defined as 'women and children', but during its implementation more specific targeting measures were introduced. The other three projects' objectives were formulated in terms of technical outputs, but it appears that mostly disadvantaged categories of the population have benefited from these projects.

**OBSERVATIONS****Targeting the poor**

11. The 1992 ALA Regulation set out a policy of targeting development cooperation on the poorest sections of the population. During the period covered by the audit, the Commission had not developed definitions or indicators to describe or identify further the intended target groups, either at the overall policy level, or in the Commission's strategy document for India of 1994.

13. Under the education sector programme specific achievement targets were set for girls and Scheduled Caste and Scheduled Tribal children. During the implementation period the definition of disadvantaged groups was enlarged to include working children and the disabled. Close attention was paid to these target groups by the regular review missions, which monitored the sector programme.

<sup>(1)</sup> This was the case in the two rural development projects Doon Valley and BAIF, the education sector programme DPEP and the NGO-led education project PESLE.

14. The programme not only established more than 28 000 schools in the EC and World Bank-supported districts of the (former) State of Madhya Pradesh for about 1,2 million children, but also introduced educational reforms (including parents' participation) in a newly created decentralised environment. The result was a substantial increase in enrolment of children from the target group, a decrease in drop-outs and an increased literacy rate.

15. For the two rural development projects 'Doon Valley' and 'BAIF' a choice was made at the design phase to focus on improving the quality of life of poor, rural people. Subsequent choices determined the areas, villages and individual beneficiaries and the types of intervention needed <sup>(1)</sup>. Even with such a clear targeting focus from the start, continuous monitoring was necessary, as the poorest people were very difficult to reach in practice. In the Doon Valley project the objectives to stop land degradation and to improve farming methods in combination with conscious management of natural resources have been achieved in an area covering some 300 villages with a population of about 400 000 people. In the BAIF project, 26 000 families (with a final target of 33 000) have so far benefited from activities to increase agricultural production, to stimulate small-scale income-generating activities and to set up family-health-based projects (sanitation, nutrition). An important achievement in both projects was also the establishment of peoples' organisations in the villages for managing the development process.

16. The PESLE project started recently and is geared toward improvement of the quality of education. Although this has a relatively wide scope, an important number of activities explicitly target tribal or minority groups and children in urban slum areas.

17. The health-sector programme's objective was to improve the quality of public health by reforming its organisational structures and procedures, including a deconcentration of the management. Although no clear targeting of the poor was formulated in its design, an overall improvement of the public health system is expected to benefit poor people. During implementation measures were taken to direct the programme towards specific disadvantaged parts of the country, e.g. certain States with poor health indicators or urban slum areas. However, the terms of reference

for the monitoring component, under which regular reviews are to be carried out, contain no reference to specific targeting objectives.

18. The three agricultural projects <sup>(2)</sup> had defined their targets in technical terms, i.e. the number of irrigation schemes to be realised, the number of kilometres of irrigation canals or the surface in hectares of agricultural land. The number and type of beneficiaries was thus defined by the physical intervention and not the result of specific attempts to target poor people in particular.

19. The main objective of the Kerala horticulture project was to provide supplementary income to Kerala's farmers by increasing the production of horticultural crops and by improving the marketing of these crops. The project covered (as planned) some 40 000 commercial farmers, who, according to a project review mission, were not considered to belong to the poorest category of farmers in the State. The exact status of the project beneficiaries was apparently difficult to assess due to a lack of socio-economic surveys.

20. Although in the preparatory phase of the Kerala 'Minor Irrigation' project it was stressed that priority should be given to the poorer districts in the State, this did not materialise, either in the financing agreement or in the implementation phase. However, the realised area under irrigation (about 7 000 hectares against a planned total of 20 000 hectares) in relation to some 13 000 farmers involved, indicates that most of the beneficiaries are small farmers.

21. The Sidhmukh and Nohar irrigation project is a technical irrigation infrastructure project for an area of about 110 000 hectares. The project area is within a region of the State of Rajasthan, which is regularly affected by drought and is considered to be a poor area. The beneficiaries are all the farmers in the project area, who can be serviced by the gravity-based irrigation system, without further distinction.

### **Sustainability**

22. According to the EC-India Cooperation Agreement on Partnership and Development <sup>(3)</sup>, a key issue to pursue in the cooperation is the sustainability of projects and programmes. An activity is considered sustainable when it is able to deliver benefits to the target group for an extended period of time, after the main assistance has ended. The sustainability of an activity can be affected by various factors, such as technical, financial and environmental issues, by the institutional and management capacities involved, or by the policy environment surrounding the activity.

<sup>(1)</sup> For Doon Valley the target group consisted of those households which mainly rely on off-farm biomass resources (in particular the forest) to sustain their livelihood. For BAIF the target group consisted of families with an annual family income below 6 000 Indian Rupees, whereas the official poverty line at the time was defined as 11 000 Rupees.

<sup>(2)</sup> Kerala Minor Irrigation, Kerala Horticulture and Sidhmukh and Nohar irrigation.

<sup>(3)</sup> OJ L 223, 27.8.1994, already discussed in paragraph 2.

In line with the Commission's own requirement <sup>(1)</sup>, the Court has examined whether during the preparation phase the Commission has assessed the various relevant factors influencing the sustainability of a proposed activity. In addition, the Court has examined to what extent the Commission has given continuous consideration to the sustainability issue during implementation.

23. The audit has shown that in five <sup>(2)</sup> of the eight audited projects/programmes the issue of sustainability was explicitly considered during the design phase. The environmental and institutional sustainability aspects, however, were usually not well documented in the different project proposals. In most cases sustainability, particularly the institutional aspect, received more consideration during the implementation. This can be seen from the various activities undertaken in all the projects/programmes to involve beneficiaries and to mobilise local communities by encouraging them to set up various types of beneficiaries' organisations.

24. In the case of the Kerala Minor Irrigation Project (KMIP), sustainability issues received explicit attention in the design, for example the economic feasibility of schemes, the importance of operation and maintenance of schemes and the planning of farmers' involvement.

25. The project experienced serious delays in achieving its physical targets during the first three years, due to the institutional weakness of the State government implementing agency. Even after the project was extended, more attention was given to the construction of additional schemes than to consolidation activities such as training farmers in operation and maintenance. As a result, at the end of the project more than 60 % of the established beneficiary farmers' associations were deemed still to be dependent on support from the project. Their chances of survival are therefore far from certain.

26. In the Kerala Horticulture Development Project (KHDP) sustainability issues were not an obvious feature of the design phase. They received greater emphasis in the two-year work plan for the extension period. In practice the project followed a participatory approach by establishing self-help groups of beneficiaries, which, in principle, should help to improve its chance of sustainability.

27. The project has achieved most of its immediate targets. However, the future activities of the recently established follow-up structure to the project, the Vegetable and Fruit Promotion Council of Kerala, were not clear at the time of the audit visit in March 2002, with several important issues still awaiting clarification and/or decision. Similarly, the financial sustainability of the agro-processing factory established under the project was far from certain.

28. The main sustainability issue for the Sidhmukh and Nohar Irrigation Project relates to the future maintenance of the newly constructed irrigation canals and related structures. As responsibility for the maintenance of the primary and secondary canals lies with the Irrigation Departments of the participating States, this will depend on sufficient budgetary allocations by the respective States.

29. In the same project it was planned to set up water users' associations, and make them responsible for part of the maintenance and to charge water users' fees. However, this was not organised during the project period, and the irrigation department intended to involve farmers only once water was flowing through the channels. As for financial sustainability, the water charges that are to be collected have initially been set at such a low level that they will only cover about 25 % of the maintenance cost.

30. The two rural development projects Doon Valley and BAIF have been the best examples among the audited activities of working towards sustainable development. They included features such as community participation in planning and implementing activities, community organisation, promotion of sustainable management practices and support in establishing income-earning activities.

31. The health sector programme's focus on institutional sustainability is clear, with its emphasis on various capacity-building measures. However, it is noted that the institutional cooperation component, foreseen in the financing agreement, only started in April 2002, i.e. in the fourth year of the programme's operation.

32. In the case of the education sector programme, sustainability was not a stated objective at the design stage. However, sustainability became an important concern during the implementation and through the review missions. The programme achievements in Madhya Pradesh, the State which actually benefited from the EC funds, were considerable. The institutional reforms carried out in the State and the State's commitment to provide education for all children mean that the outlook for sustainability in Madhya Pradesh is promising.

<sup>(1)</sup> According to the project cycle management methodology, adopted in 1992 by the Commission, financing proposals for projects/programmes should include an assessment of sustainability. See also the Court's Special Report No 21/2000 on the management of the Commission's external aid programmes, paragraphs 28 to 30 (OJ C 57, 22.2.2001). (The financing proposal for a development project or programme is the internal Commission document, prepared by Commission staff and presented to the Advisory Committee of Member States' representatives, on which the financing decision of the Commission is based.)

<sup>(2)</sup> Kerala Minor Irrigation, Sidhmukh and Nohar Irrigation, Doon Valley, BAIF and the health sector programme.

33. Financial sustainability of the national programme remains a longer-term issue, especially given that States, many of which are having fiscal difficulties are expected to contribute 25 % (up from 15 %) of the funds necessary for the new programme.

34. In the Programme for the Enrichment of School Level Education (PESLE) consideration of sustainability issues is so far not well developed. The local core partners are mostly small NGOs whose financial sustainability is not guaranteed. Even though in some cases the quality of work is considered very good, the real difficulty is to mainstream any improved methods and innovative strategies into larger education systems.

35. The Court found that in most of the activities audited developing sustainable structures was a crucial factor determining whether or not individual project/programme achievements will be continued over a period of time. Thus, the earlier the organisation of community participation was undertaken and built into the project approach, the better the prospects for a sustained impact at the end of the project/programme.

36. An issue which the Court found to have an impact on sustainability is the planned duration of projects/programmes. The majority of the projects/programmes examined went through one or more extensions of their implementation periods. Even with such extensions several projects still came under time pressure towards the end. It appears that the period of time needed for implementation is systematically underestimated in the preparation phase. When project periods are subsequently extended, the administrative process that arranges this is usually slow and cumbersome, often having a negative impact on project implementation. Also, projects under time pressure tend to give priority to attaining short-term, physical targets, at the expense of longer-term, and possibly less visible, factors, such as institutional capacity building <sup>(1)</sup>.

37. In this respect it should be noted that the EC's revised Financial Regulation <sup>(2)</sup>, which applies from 1 January 2003, contains a provision limiting the period during which contracts may be concluded. This is likely to reduce the implementation period allowed for development cooperation activities. In its opinion on the proposal for the new regulation, the Court considered this to be unsuitable in the context of development aid because the maximum implementation period seems too short <sup>(3)</sup>. In the light

<sup>(1)</sup> For example KMIP, see paragraph 25.

<sup>(2)</sup> Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities, Article 166 (OJ L 248, 16.9.2002).

<sup>(3)</sup> Court of Auditors, Opinion No 2/2001 on a proposal for a Council Regulation on the Financial Regulation applicable to the general budget of the European Communities, paragraph 63 (OJ C 162, 5.6.2001).

of the above arguments, the new provision will generally make it more difficult to build sustainability into the activities.

### *Sector-wide approach and coordination*

38. It is generally accepted by the Commission <sup>(4)</sup>, as well as by many other donors, that a sector-wide approach to certain development cooperation activities is in principle preferable to the more traditional project-based approach as it encourages more harmonisation and coherence in sectoral policies and strategies. Nationwide sector programmes, such as those supported by the Commission for education and health in India, offer the advantage of reaching much larger numbers of people, and thereby having a much wider impact. As these programmes are implemented and supported through existing government channels, with funds provided in central and State governments' budgets, the local ownership of such sector programmes increases the chances of sustainability.

39. Under a sector-wide approach all interested parties jointly agree to support and finance a particular sector programme with the government responsible for implementation. Donors contribute to the programme often without earmarking their funds for specific components. The government together with the donor community formulates the objectives, the target groups and the organisation of the programmes, including issues like definition of performance indicators, disbursement conditions and mechanisms on monitoring, reporting and auditing.

40. By refraining from a multitude of arrangements for each of the donors, a more efficient process is possible under a sector-wide approach than in a donor-fragmented project approach. A consequence of this approach is that donors cannot trace how their funds have been used specifically. Donors should therefore have sufficient confidence in the capacity of the beneficiary country's administration to manage sector-wide programmes and to account for their implementation, results and costs.

41. However, the audit has shown that there has not been a full-fledged sector-wide approach in the national education and health sector programmes. In India, only the EC has so far supported a subsector programme approach with budgetary aid. All other donors, while supporting the same sectors, have operated through a project-based approach, allocating their funds to specific components and/or geographic destinations, to ensure a direct control on the utilisation of their funds.

<sup>(4)</sup> See the Commission's Communication COM(2000) 212 final on the EC's development policy.

42. As a result, it has not been possible to establish common accountability and reporting arrangements for the nationwide programmes in education and health. In the case of the education programme this constraint was largely overcome by allocating the largest part of the EC funds to this sector through a body specifically created for the duration of the programme in one single State. For the health programme no such arrangement was made and it is to be noted that the Commission had not been able to obtain from the Government of India up-to-date and audited financial statements on the overall health programme.

43. The main coordination activity for the education programme has been a system of semi-annual joint review missions, whereby teams of donor and government representatives visit programme activities in a selection of participating States. This system of joint reviews was generally deemed to have a positive effect on the implementation of the programme, as it brought together a pool of expertise and allowed the Commission and other donors to look at the programme as a whole, rather than just at the States that received finance from them. Otherwise coordination has been on an informal basis.

44. In the case of the health programme no such system of joint reviews or other formal coordination mechanisms involving other donors exist. The Joint Steering Committee, set up under the EC-India agreement on this programme, could have become an effective coordination instrument, as other donors are also invited to attend, but in practice it is mainly a meeting place for Indian and EC representatives and technical advisers. Informal meetings of donors involved in the health sector have taken place.

### *New country strategy*

45. With poverty reduction as the central objective of the Community's development policy <sup>(1)</sup>, the Commission has recently identified a need to address rural development concerns more systematically and comprehensively <sup>(2)</sup>. This is because, as it has been stated, poverty and hunger are mainly rural problems, and environmental degradation is becoming increasingly severe in rural areas and is closely connected to rural poverty. In order to tackle rural poverty several sectors need to be addressed, of which agriculture, health and education and natural resources management are of particular importance. The communication then goes on to present the EC's policy and approach to rural development in developing countries, integrating the objectives of poverty reduction, food security and sustainable natural resources management into a coherent framework.

<sup>(1)</sup> COM(2000) 212 final, page 5; see also the European Community's Development Policy — Statement by the Council and the Commission, 10 November 2000.

<sup>(2)</sup> COM(2002) 429 final: Communication from the Commission on fighting rural poverty.

46. However, the Commission has not fully followed this approach when designing its new country strategy for India. The Commission has proposed to focus its support to India for the next five-year period in particular on the health and education sectors. Even though poverty in India is described as a predominantly rural phenomenon, with three out of four poor people living in rural areas <sup>(3)</sup>, the Commission's strategy does not address specific rural poverty problems in the areas of agriculture and natural resources management.

47. The Court's audit findings confirm the Commission's own judgement <sup>(4)</sup> that some of its rural and natural resources development projects in India, especially the more technically oriented ones, may have uncertain prospects for sustainability. However, the two rural development projects examined can be considered as quite successful in terms of achieving sustainable development for the very poor in a direct way. Both projects have undertaken a variety of activities aimed at the different aspects of rural poverty, such as increasing the productivity of land and water, natural resources management, family health and community health activities, empowerment of women and community participation. However, the new strategy does not indicate whether any follow-up will be given to these successful rural development projects.

## CONCLUSIONS AND RECOMMENDATIONS

### *Overall conclusion*

48. The Court concludes that the Commission's management has been reasonably successful in targeting the poor and in building in sustainability for the majority of the eight projects/programmes audited in India. More systematic attention for these issues throughout the whole project/programme life cycle could, however, have improved the results.

49. Extensive donor coordination efforts have taken place to establish a system of joint review missions within the education sector programme. Nonetheless, the EC has so far been virtually alone in fully supporting a sector programme approach in India and in this respect present donor coordination leaves considerable scope for improvement.

<sup>(3)</sup> The EC-India Country Strategy Paper 2002 to 2006, paragraph 3.2.2.

<sup>(4)</sup> EC-India Country Strategy Paper 2002 to 2006, paragraph 4.1.

### **Targeting of the poor needs explicit attention at all stages**

50. Specific objectives and/or measures to target poor, disadvantaged groups were included in three of the six projects, in the education programme and, albeit more indirectly, in the health programme.

51. In particular, the rural development projects offered clear opportunities for direct individual targeting of poor people. However, for a number of other projects, the choice of a certain type of intervention because of related technical or geographical limitations (e.g. irrigation) reduced the scope for targeting specific groups of beneficiaries.

52. Sector programmes offer the advantage of reaching far greater numbers of beneficiaries and, potentially, much larger target groups. In sector programmes, by nature different from projects, individual activities are not always well defined at the outset. This means that during implementation specific measures have to be taken to ensure that the programmes' benefits will reach the intended beneficiaries.

#### *Recommendation 1*

53. The objective of targeting the poorest sections of the population should be incorporated and operationalised from the very beginning of the identification phase and it should continue to be pursued during the implementation phase. Monitoring and evaluation activities need to focus on the effectiveness in respect of targeting the poor.

### **Sustainability would benefit from more systematic attention and realistic planning**

54. In five of the eight projects/programmes audited sufficient attention was given to sustainability aspects during the design phase. In most cases attention improved during implementation, especially as regards the institutional sustainability aspect. All the projects/programmes audited had worked towards setting up various types of beneficiaries' organisations, but the sustainability of such institutions was a weak point.

55. In most cases time estimates for the required implementation period were too optimistic, leading to an increased focus on completing the short-term physical targets and to requests for extension of the implementation period. Although extensions

would usually be in the interest of the projects/programmes and their chances of sustainability, their administrative processing was generally slow and cumbersome, with a negative impact on implementation.

#### *Recommendation 2*

56. All relevant aspects of the sustainability of projects/programmes should be given explicit and detailed attention from the design phase onwards and should be closely monitored throughout the implementation period. Chances of sustainability would improve if projects/programmes, especially when involving institutional capacity building or reforms and human resources development, were allowed an appropriate implementation period from the outset in combination with regular reviews being carried out. A specific phasing-out period for implementing a clear exit strategy should also be included.

### **Sector-wide approach needs closer donor coordination**

57. A sector-wide approach offers certain advantages over a project-based approach, including the potential for a more harmonised and coherent set of policies and strategies, wider impact, more local ownership and better chances of sustainability. Such an approach also requires that donors have sufficient confidence in the capacity of the beneficiary country's administration to manage sector-wide programmes and to account for their implementation, results and costs. However, in practice there was no sector-wide approach, and therefore no common reporting, accounting and auditing systems, in the nationwide education and health sector programmes. For the education programme this constraint was overcome by the allocation of the EC funds to a single State and by the creation of specific structures in that State. For the health programme no such arrangement was made and the Commission had not been able to obtain from the Government of India up-to-date and audited financial statements on the overall health programme.

58. In the case of the education sector programme inter-donor coordination took place through a well-appreciated system of biannual joint review missions. For the health sector more informal channels for coordination were used.

#### *Recommendation 3*

59. When considering contributing to a sector programme through budget support, the Commission (together with other donors) should ensure both beforehand and — later — in the course of implementation, that the direction on public finance (including reporting, accounting and auditing systems) taken by

the country concerned is satisfactory <sup>(1)</sup>. Where necessary, support to build up institutional capacity in these areas should be provided in addition to the specific sector support. In a situation where capacity building is unlikely to ensure adequate accountability for unearmarked budget support, the Commission should consider other forms of support.

***Agriculture and natural resources management to remain part of country strategy***

60. The new EC-India country strategy paper does not fully apply the approach outlined in the Commission's recent communication on fighting rural poverty, as it limits EC intervention to the health and education sectors, leaving aside other key sectors

(agriculture, natural resources management) identified in that communication as needing to be addressed if rural poverty is to be tackled successfully.

*Recommendation 4*

61. In the light of its overall poverty reduction objective the Commission could make its new EC-India country strategy more comprehensive by addressing important issues like agriculture and natural resources management. Successful approaches in these areas, as developed in some of the Commission's projects, could be promoted as models, to be applied in the government's own poverty reduction strategies and programmes.

This report was adopted by the Court of Auditors in Luxembourg at its meeting of 19 June 2003.

*For the Court of Auditors*  
Juan Manuel FABRA VALLÉS  
*President*

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<sup>(1)</sup> Similar observations have been made by the Court in its Special Reports concerning structural adjustment facilities and macrofinancial assistance: Special Report 5/2001 on counterpart funds from structural adjustment support earmarked for budget aid (OJ C 257, 14.9.2001); and Special Report 1/2002 on macrofinancial assistance to third countries and structural adjustment facilities in the Mediterranean countries (OJ C 121, 23.5.2002). In May 2002 the Commission's EuropeAid Cooperation Office adopted a guide on the management of budget support operations, which recommends such prior verification of local conditions before granting budget support.

## THE COMMISSION'S REPLIES

### SUMMARY

I. In 30 years of development cooperation with India the Commission's strategy has evolved from support financed through counterpart funds (e.g. Operation flood) and rural development projects to sector programmes in health and education which support the Government's reform agenda, good governance and improved service delivery. The decision to move away from the classical rural development projects was based on the experience that individual projects, although often achieving the objectives, tended to have limited and localised impact, with little influence over policy.

Community cooperation with India has therefore benefited from a dynamic learning exercise, whereby experiences from ongoing projects have fed into the development of new strategies.

IV. Commission-managed programmes in health and education aim, *inter alia*, to encourage the Indian authorities to move towards a sector-wide approach in addressing social development issues. In this framework, efforts are made to enhance donor coordination, to reduce transaction costs and to increase aid effectiveness. A key to progress in this area is increased Government ownership which can be built up through capacity building and dialogue. The Commission's guidelines on sector-support programmes adopted in February 2003 attach particular importance to donor coordination. The intensification of this coordination will be a key task for the newly devolved Delegation of the Commission in India.

In the case of the sector programme of Support for District Primary Education Programme (DPEP), and the Support to Health and Family Welfare Support Programme (HFWSP), arrangements in relation to reporting, accounting and auditing are carried out in accordance with the financing agreement signed between the Commission and the Indian Government.

Widening these arrangements towards a common framework incorporating all donors in the sector is part of the ongoing dialogue. The establishment of such a framework will be facilitated, notably in the health sector, by a move by other key donors from a project to a sector-wide approach.

V. Inadequate health and education facilities are key aspects of rural poverty and it is now generally agreed by all donors in India that by strengthening these two sectors a maximum impact on poverty reduction can be achieved. By selecting these two sectors as priority areas of its new strategy (which received strong support from the EU Member States), the Commission aims to achieve maximum impact without diluting its efforts in too many different sectors or approaches. Moreover, important synergies are expected to be created with the ongoing sector programmes in health and education in the future partner States.

The Commission's development communication identifies six key sectors for poverty reduction but this does not mean that all six need to be taken on board for each new programme. The policy gives the Commission the possibility, in dialogue with the recipient country, to agree on the sectors that are most appropriate for the country in question.

VI. The Commission takes note of the Court's recommendations concerning the objectives of targeting the poorest sections of the population and sustainability.

Since 1992 the Commission uses the 'Methodological guide' and other project cycle tools such as the logical framework approach. It is therefore now standard practice to build sustainability aspects (including exit strategies) into Community development projects and programmes.

The Commission takes note of the Court's recommendation on sector programmes which is being implemented both under the Guide to the programming and implementation of budget support for third countries adopted in March 2002 and the Guidelines for European Commission Support to Sector Programmes adopted in February 2003.

The Commission considers that there are strong reasons for concentrating its resources on the health and education sectors. In addition, the future State partnerships that the Commission intends to develop should provide a holistic reform package which could add a rural and natural resource dimension to the education and health activities.

## INTRODUCTION

3. Over 30 years of development cooperation with India, Community strategy has evolved from rural development projects and counterpart funded support (e.g. Operation flood) to sector-support programmes in health and education which support the Government reform agenda, good governance and improved service delivery. The decision to move to sector-support programmes resulted from the experience that individual projects, whilst often achieving set objectives, tend to have a limited and localised impact, with little influence over policy.

6. In a economy the size of India, it is not the amount of aid that is so critical as the fact that the Commission is engaging in dialogue with a major world player and partner about larger policy issues (of which education and health policy are part).

## OBSERVATIONS

11. Article 4 of the 1992 ALA Regulation (Financial and Technical Assistance to Asia and Latin America) states that Community aid shall target primarily the poorest sections of the population. It furthermore identifies women, children and ethnic minorities as warranting special attention.

15. The Commission agrees with the Court that 'Doon Valley' and 'BAIF' both constitute good examples of including 'targeting the poor' and 'indicators' in the design phase.

17. The purpose of the health sector reform and programme is not to develop a special health system for the poor, as experience proves that this generally results in a poor health service. 'Improving the quality of the public health system' has therefore from the outset focused inherently, in operational terms

as well as in monitoring terms, on making the existing system more accessible, affordable and adequate to the poor, particularly where it is currently weak in this respect (e.g. slum areas, backward States). The allocation of 50 % of the balance funds under the Sector Investment Programme for the fiscal year 2001/02 to the most needy States is a further illustration of this key inherent concern of the programme.

18 and 19. The Kerala Minor Irrigation, Kerala Horticulture and Sidhmukh and Nohar Irrigation projects were proposed to the Commission as technical interventions designed to address the needs of beneficiaries in poorly developed areas. It is inherent in the nature of the physical intervention — in this case infrastructure investments — that a pure targeting of below-poverty-line beneficiaries and an exclusion of the above-poverty-line populations from the benefits of the intervention (irrigation) cannot take place. It is now recognised by all donors in India that there is a need to build much more proactive mechanisms for ensuring more equitable benefit distribution in such infrastructure projects.

This is the reason why the Commission has moved away from this approach. In the more recent projects, the poor are explicitly targeted and baseline surveys and participatory assessments are usually factored into a 'Year 0' of project implementation.

20. The Kerala Minor Irrigation project is an old one where more attention was given to meeting technical targets (see also point 18). However, indirectly the project managed to target the small landholders which belong to the poor.

Poverty targeting has been more focused in recent programmes

22 and 37. The Commission is pleased to note that the Court concluded (paragraph III of the summary) that the Commission's management has been reasonably successful in addressing sustainability.

26 and 27. The institutional structure of the Kerala Horticulture Development Project was transformed during the course of the project. The Commission has taken initiatives to ensure the financial sustainability of the agro-processing factory. As a result, the factory has been able to get the highest level of certification and is well poised to ensure future growth.

The delegation is organising a final evaluation in September 2003 and is continuing its dialogue with the VFPC (Vegetable and Fruit Promotion Council of Kerala) and the NACP (Nadukkara Agro Processing Company) with a view towards supporting both in seeking to achieve financial sustainability.

29. Recovery costs were kept at a level commensurate with the project beneficiaries' ability to pay.

31. The institutional cooperation component of the health-sector programme is now well on track. The start of this component was dependent on the development and approval by all parties concerned of the sector investment programme that laid the basis for the process of reform and identified the different institutional entities (existing or to be created) concerned by the reform.

33. It is the policy of the central Government through centrally sponsored schemes to foster progressively fiscal and public finance reform at State level. The Commission supports this policy.

34. The Commission is aware of sustainability issues in the Enrichment of School Level Education Programme (PESLE) and this will be addressed in detail during the consolidation phase.

35. Since 1992 developing sustainable structures and involving the community is common practice in Community development policy.

36 and 37. To avoid problems with requests for extensions more recent projects and also the sector programmes were designed with a longer implementation period (e.g. BAIF: nine years, SSA: seven years).

37. The deadline for signing contracts (Financial Regulation, Article 77(2) and 166(2) (sunset clause)) and the deadline for implementation (Financial Regulation Article 77(3)(1)) are two different elements. The Commission considers both deadlines to be essential tools for ensuring sound financial management and more efficient budget implementation.

The abovementioned provisions were adopted by the Legislative Authority; the Commission is committed to respect the new regulation and is making major efforts to improve implementation of external actions and to reduce the backlog of old and dormant commitments. These new rules are much-needed tools in view of reaching these objectives.

40. Donors should also be ready to assist beneficiary countries to strengthen their capacity to manage sector-wide programmes. This is a key feature of donor support to sector-wide approaches.

42. For the Community health programme the financing agreement states that regular auditing will be carried out under the Government of India procedures. The Commission accepts the Court's observation that this arrangement has not been found satisfactory in ensuring availability of timely and adequately audited financial statements for this programme. The Commission therefore requested the mid-term review to look into this matter and to provide recommendations on how accountability and reporting arrangements could be improved. The Commission received the draft report of the mid-term review in April 2003. The report does contain a number of concrete recommendations in this respect, which the Commission is in the process of discussing with the Government of India.

44. Donors active in the health sector like the World Bank, DFID, USAID and SIDA are invited regularly by the Ministry of Health to the Joint Steering Committee meetings of the Community programme. However, the response of the donors has generally been low key as none of them fund on a sector-wide basis. Informal coordination mechanisms have been set up and all donors and senior representatives of the Department of Family Welfare regularly attend. On a formal basis, greater donor coordination is taking place at the State and District level.

Currently, there is an increasing consensus among the donor community about the need for reforms in the health sector. There are good indications that other donors would in future pursue the reform strategy and participate in coordinated sector support.

46. Inadequate health and education facilities are key aspects of rural poverty and it is now generally agreed by all donors in India that by strengthening these two sectors a maximum impact on poverty reduction can be achieved. By selecting these two

sectors as priority areas of its new strategy (which received strong support from the EU Member States), the Commission aims to achieve maximum impact without diluting its efforts in too many different sectors or approaches. Moreover, important synergies are expected to be created with the ongoing sector programmes in health and education in the future partner States.

The Commission's development communication identifies six key sectors for poverty reduction but this does not mean that all six need to be taken on board for each new programme. The policy gives the Commission the possibility, in dialogue with the recipient country, to agree on the sectors that are most appropriate for the country in question.

47. In all cases, Community projects are followed up through final evaluations. The results will feed into the new strategy.

## CONCLUSIONS AND RECOMMENDATIONS

51. The project approach per se has geographical and thematic limitations with respect to targeting the poor and the Commission is therefore moving towards a more holistic approach to its poverty reduction strategy (State partnerships and sector-support programmes).

52. Sector programmes are disbursed against achieved benchmarks for policy reform measures, not against individual activities. Monitoring indicators should show whether the poor have been reached and benefited from the programme. Therefore, outcomes rather than inputs and activities are stressed in the sector approach.

### *Recommendation 1*

53. In line with Community Development policy and guidelines, the targeting of the poorest sections of the population is common standard practice for all programmes and projects in India and other countries.

54. Within a project approach it is difficult to guarantee sustainability of beneficiary organisations beyond the life of a project. A sector-programme approach addresses this issue more adequately through building ownership and increasing coherence between objectives, spending and results.

55. In the context of its reform of the management of external assistance, the Commission, through devolution to its Delegations in the field and accompanying quality measures, attaches special importance to greater realism in project/programme design. This concerns in particular the setting of objectives and accompanying implementation timeframes.

### *Recommendation 2*

56. Since 1992, the Commission uses the 'Methodological guide' and other project cycle tools such as the logical framework approach. It is therefore now standard practice to build sustainability aspects (including exit strategies) into Community development projects and programmes.

57. Donors should also be ready to assist beneficiary countries to strengthen their capacity to manage sector-wide programmes. This is a key feature of donor support to sector-wide approaches.

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### *Recommendation 3*

59. The Commission agrees with the Court's recommendation which is being implemented both under the Guide to the programming and implementation of budget support for third countries adopted in March 2002 and the Guidelines for European Commission Support to Sector Programmes adopted in February 2003.

60. Inadequate health and education facilities are key aspects of rural poverty and it is now generally agreed by all donors in India that by strengthening these two sectors a maximum impact on poverty reduction can be achieved. By selecting these two sectors as priority areas of its new strategy (which received strong support from the EU Member States), the Commission aims to achieve maximum impact without diluting its efforts in too many different sectors or approaches. Moreover, important synergies

are expected to be created with the ongoing sector programmes in health and education in the future partner States.

*Recommendation 4*

The Commission's development communication identifies six key sectors for poverty reduction but this does not mean that all six need to be taken on board for each new programme. The policy gives the Commission the possibility, in dialogue with the recipient country, to agree on the sectors that are most appropriate for the country in question.

61. As pointed out in the reply to paragraph 60, the Commission considers that there are strong reasons for concentrating its resources on the health and education sectors. In addition, the future State partnerships that the Commission intends to develop should provide a holistic reform package which could add a rural and natural resource dimension to the education and health activities.

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