

**UPDATED DISCUSSION PAPER ON THE CORE BUSINESS MODEL OF A MATURE
GLOBAL FUND**

Outline: This report is an updated version of a discussion paper circulated to the Eighth Board Meeting (GF/B8/13, "Discussion Paper on the Core Business Model of a Mature Global Fund"). It includes an additional section covering the background analysis that had previously been presented to the Board separately (through Board Updates prior to the Eighth Board Meeting). The section in the earlier discussion paper on improvements to the current business model has been removed, as it covered changes (such as the reorganization of the Secretariat, the codification of core business practices, the mainstreaming of performance management systems at the Secretariat, and the development of a framework to systematically identify risk and manage it through differentiated approaches to portfolio management) that have largely been operationalized by the Secretariat in the intervening months. This report is provided to the Board as a contribution to the discussions that will take place at the Board Consultation on 20 November 2004.

Part 1: Introduction

1. The Global Fund has grown explosively in its first two years of existence. By the end of 2002, the organization had approved an initial set of 56 proposals in 37 countries worth US\$567 million, and had just begun to sign the first grant agreements and disburse a few hundreds of thousands of dollars. A year later, the end of 2003 saw a much larger Global Fund, with 224 components having been approved in 121 countries, totaling US\$2.1 billion. Grant agreements had been signed in 77 countries and disbursements worth US\$232 million had been made. By mid-2004, 297 components had been approved in 128 countries, totaling US\$3.1 billion. At the time of finalizing this report, 224 grant agreements have been signed in 120 countries, representing a value of US\$1.9 billion, and disbursements totaling US\$631 million had been made. The first results of these resources are starting to be seen, with Global Fund financing being used to scale up prevention, care, and treatment interventions across the world.

2. The Secretariat has developed a forecast of the organization's medium-term growth to underpin a thorough analysis of our business model. These projections, and the implications that they have for the ability of the Global Fund to fulfill its mission, have prompted the Secretariat to examine options for the future. Considerable effort is underway at the Secretariat to make improvements within the current business model, topics that are not addressed herein. Instead, this report focuses on two key areas:

- a. Changing core aspects of the current business model; and
- b. Addressing gaps in the architecture to respond to requests from recipients and partners.

3. In preparing this analysis, the Secretariat was guided by a number of key principles, as originally articulated in the Framework Document. First and foremost, any changes to the organization's architecture must enhance our ability to serve the recipients of Global Fund financing, both those who will directly utilize Global Fund monies and the broader array of people and communities living with, affected by and at risk from AIDS, tuberculosis and malaria. A corollary of this is that the Global Fund must step up efforts to achieve smooth harmonization with existing systems, rather than establishing parallel requirements. In too many countries, Global Fund financing is perceived as replete with its own conditions, rather than as a mechanism that seamlessly funnels resources into the scaling up of existing responses to the diseases, and modifications to our architecture should assist in rectifying this.

4. Simultaneously, reengineering should improve efficiency and ensure cost-effective use of resources, both at the Secretariat and in recipient countries. In no case should change result in any lessening of the organization's commitment to accountability and quality, and to financing programs that are demonstrably benefiting people and communities living with, affected by and at risk from AIDS, tuberculosis and malaria.

5. Finally, this analysis must acknowledge and seek to address the fact that the Global Fund has yet to live up to its full potential in reaching the entire breadth of actors involved in the fight against these three diseases. The organization was established as a public-private partnership, but to date it has not been sufficiently innovative in its attempts to ensure adequate participation of all stakeholders. In particular, the basic architecture must become more conducive to facilitating the involvement of the private sector and of people and communities living with, affected by and at risk from AIDS, tuberculosis and malaria.

6. In developing this analysis, the Secretariat has drawn upon a number of sources, including the case studies carried out on Country Coordinating Mechanisms, an evaluation of Local Fund Agents, and several academic studies focusing on the Global Fund (such as the "Tracking Study" carried out by the London School of Hygiene and Tropical Medicine). A

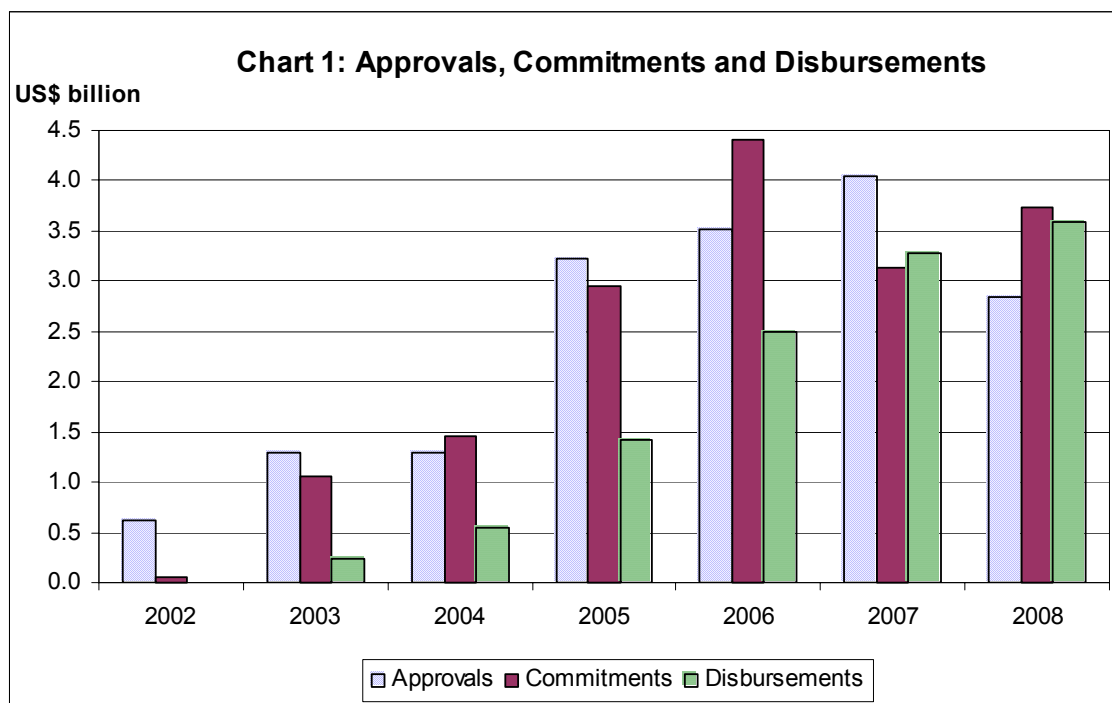
retreat bringing together the Secretariat leadership with some of the leading thinkers on development finance issues was also convened to discuss some of the propositions contained in this paper. A paper released by Steven Radelet of the Center for Global Development was also considered in the preparation of this report and has been included as an Annex (although the document was not prepared at the request of the Global Fund, but rather as part of the author's ongoing work on development assistance and aid effectiveness). Additionally, comments made during the brief discussion on the topic at the Eighth Board Meeting have been incorporated.

Part 2: Future projections

1. Future predictions of demand and supply of Global Fund resources are limited to best estimates, given that the Global Fund operates through a demand-driven proposal process and with voluntary donations. However, building upon the organization's first two and a half years of experience and using a few key assumptions, the forecasts below sketch out a picture that should not be too far from reality if the Global Fund pursues its current business model.
2. The key assumptions in this forecast include that:
 - The Global Fund will launch three rounds of proposals every two years, with each Round resulting in US\$1 billion in new proposals being approved for an initial two year period;¹
 - Each new Round of proposals is expected to generate 100 new grants out of which 85% will be renewed for Phase 2.
3. Based on these key assumptions, the Global Fund is expected to reach a "steady state" of operations by 2008 (referred to as a "cruising altitude" in some previous communications), in which the number of new proposals is balanced by the number of proposals reaching the end of their five-year lifespan.
4. These assumptions are conservative and result in a steady state that is considerably below the founding vision of a Global Fund channeling US\$7–10 billion per year to dramatically scale up the responses to AIDS, tuberculosis and malaria. They also imply that the Global Fund's share of global financing will decline, as needs expand while Global Fund resources reach a plateau. Whether this vision of a steady state is in keeping with the enormity of the task of responding to three deadly pandemics that led the international community to set up the Global Fund is a topic that requires further discussion, but that is outside the scope of this paper.
5. When the Global Fund reaches its steady state in 2008, each year will feature, on average:
 - 150 new proposals approved (with a range of between 100 and 200, reflecting the approval of three Rounds every two years);
 - 150 requests for Phase 2 renewal received;
 - 280 grants signed (including both Phase 1 grants and Phase 2 grant extensions); and
 - 1400 disbursements made.

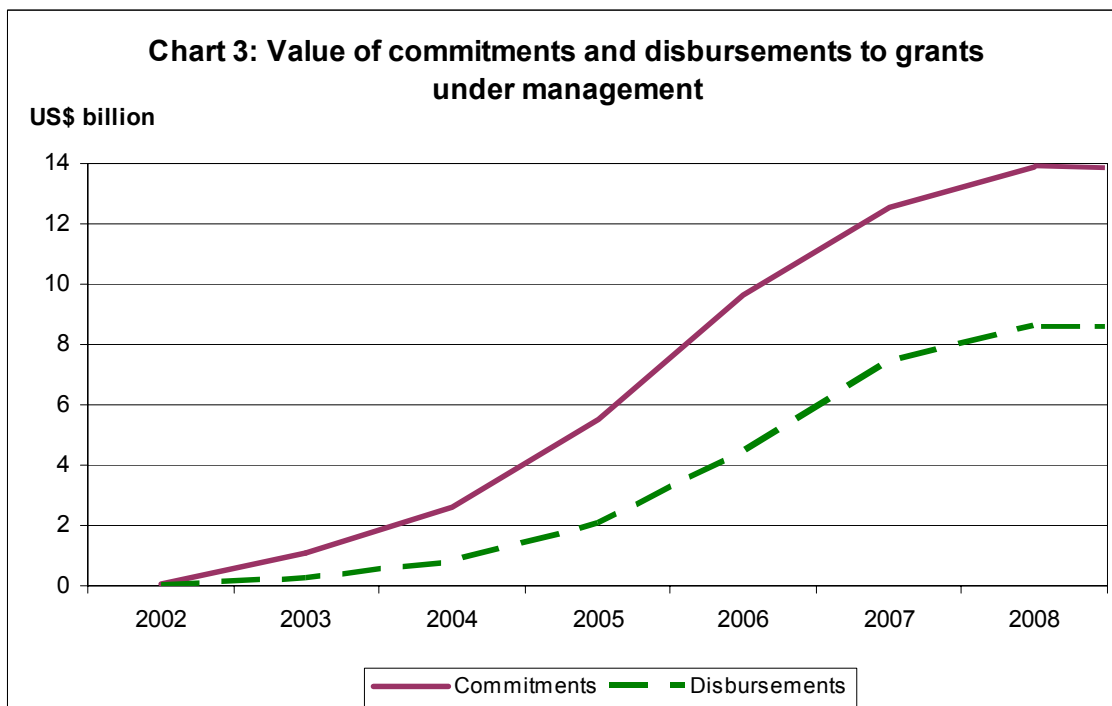
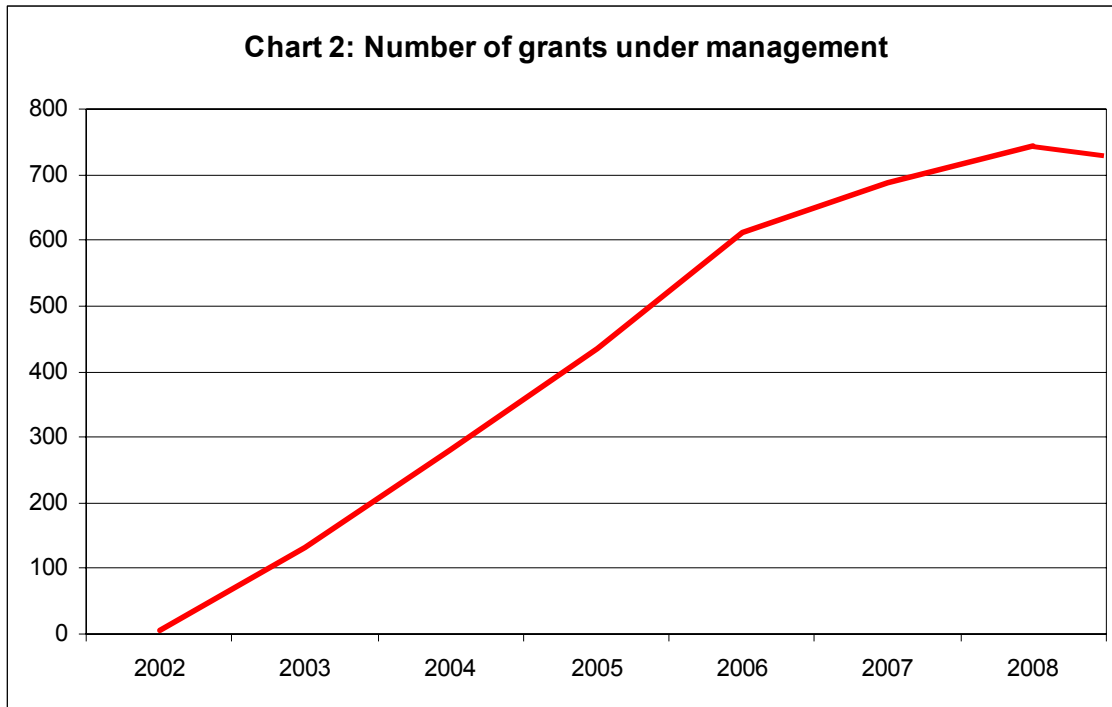
¹ The frequency of Rounds and the related question of their size are based on current practice, and need to be considered in tandem: should the frequency of Rounds decrease, the average size of a Round might well increase.

6. As shown in Chart 1, the annual values of approvals (including both Phase 1 and Phase 2), of commitments (for grants signed) and of disbursements will peak at roughly US\$4.0 billion, US\$4.4 billion and US\$3.6 billion respectively, before reaching a steady state of approximately US\$3.3 billion each from 2008 onwards.²

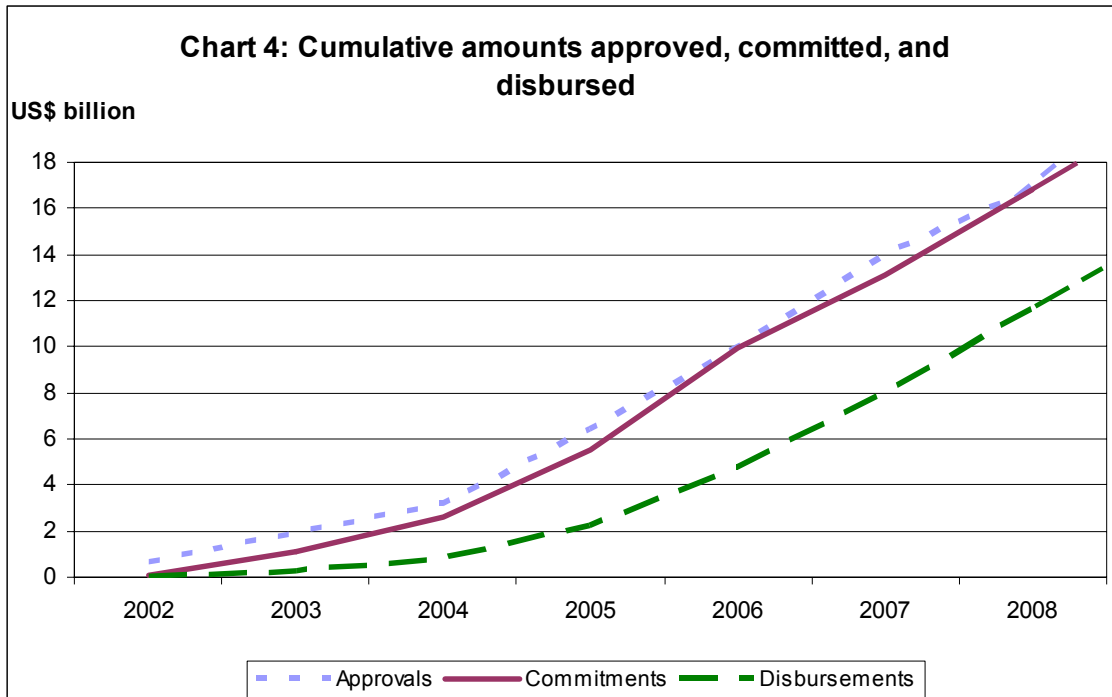


7. In 2008, nearly 750 grants will be under active management, after which time the number of active grants declines slightly to a steady state of approximately 700 by year. The grants under active management in 2008 have a total value of US\$13.9 billion, with US\$8.6 billion having been disbursed to these grants. Charts 2 and 3 show the increase in the number of grants under active management, and the total funds committed and disbursed to these active grants, respectively.

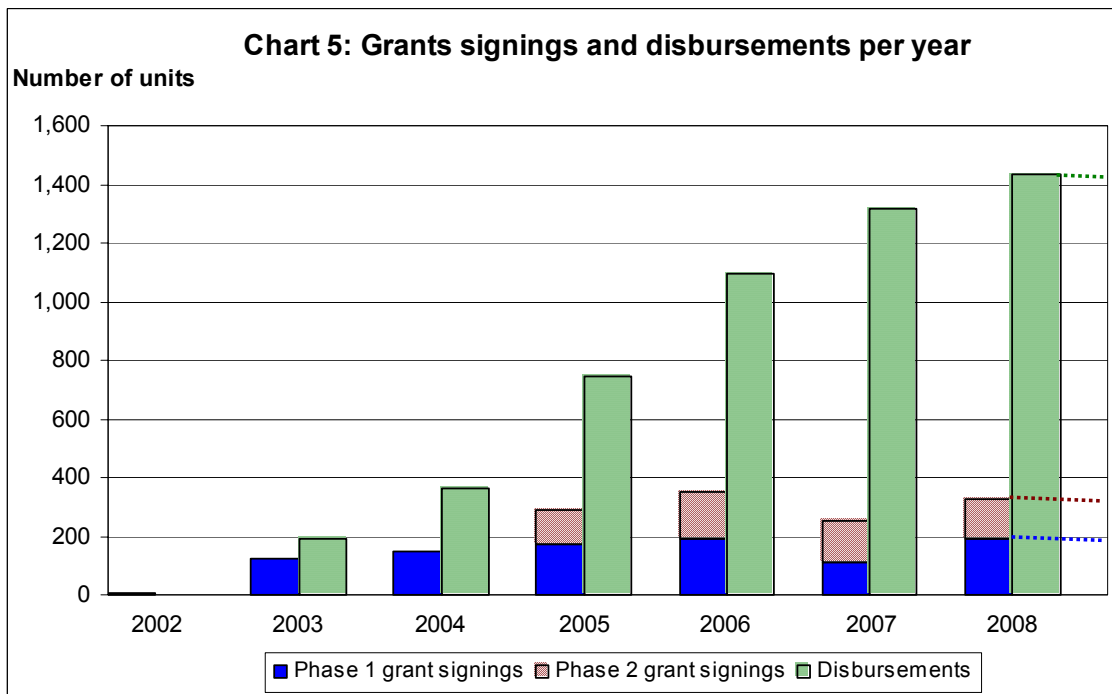
² This steady state is slightly higher than earlier estimates, as a result of refinements to the model, additional information on approvals, commitments, and disbursements, and slightly more conservative assumptions (e.g., on savings in grant negotiations). By way of comparison, a scenario in which one Round of proposals was approved per year and the average size was assumed not to adjust for this (i.e., to remain at US\$1 billion), the steady state of approximately US\$2.2 billion would be reached in 2008.



8. Turning to the cumulative amounts of all Global Fund approvals, commitments, and disbursements since inception (incorporating both active grants and those that will have already reached the end of their five year lifespan), a total of nearly US\$17 billion will have been approved and committed and US\$11.6 billion will have been disbursed by 2008, as depicted in Chart 4.



9. This rising volume of activity has considerable implications for Secretariat workload, as the grant is currently the basic unit of work for portfolio management. While there are some economies of scale, under the Global Fund's current system certain tasks must be carried out for each grant under management. These include the activities around grant signing, the analyses and reviews associated with making performance-based disbursements, and the recommendations for Phase 2 renewals and negotiations of Phase 2 grant extensions. Chart 5 shows the increases in these areas to 2008.



10. Chart 5 shows a significant increase on the current workload. To date, a total of 224 Phase 1 grant agreements have been signed, 422 disbursements have been made, and no Phase 2 grant extensions have occurred.

Part 3: Changing core aspects of the current business model

1. The current architecture of the Global Fund was largely designed in late 2001 and the first half of 2002. During the early days of the Transitional Working Group and Transitional Support Secretariat, numerous innovative ideas were proposed and debated but ultimately shelved, often due to their complexity and the need to launch the Global Fund rapidly. Some of the concepts discussed below were originally broached more than two years ago and are even contained in the Framework Document (typically as options that were never operationalized); others reflect new thinking stemming from the organization's first two years of experience.

2. It is an ideal moment to reopen the discussion into some of the fundamental structures of the Global Fund, both because of the stark picture of massively rising volumes of Global Fund transactions (which cannot be handled by a Secretariat of the current size, even through efficiency gains within the business model) and because significant lessons have been learned in the first two years of business. The possibilities for reengineering can be grouped into three broad and interrelated areas:

- a. The process of identifying programs to finance;
- b. Implementation arrangements; and
- c. Oversight mechanisms.

3. The following three subsections cover each of these topics in turn. Each subsection has the same structure, beginning with a stylized description of the current approach, highlighting some of the problems with it, and then identifying possible responses.

4. A key guiding premise that runs throughout each subsection is that the basic division between the Country Coordinating Mechanism (CCM) and the Principal Recipient (PR) should be preserved, rather than, for example, combining the two entities. Nonetheless, the current relations between the two are impacted considerably by some of the proposals. A related theme is that if the concept of the CCM is to continue to remain central to the Global Fund's operations, much more must be done to develop it and, in particular, to provide incentives to promote its performance.

A. The process of identifying programs to finance

5. Programs are currently identified periodically, in distinct Rounds of financing. In response to the announcement of a Round (the timing of which is determined by the Global Fund), CCMs submit proposals on a form that has been designed by the Global Fund. A Technical Review Panel (TRP) then convenes in Geneva and reviews each eligible proposal, without a visit to the country from which the proposal originates and often with only limited contextual information. It makes recommendations to the Board of the Global Fund and, resources permitting, technically-sound proposals are then approved for five years, but with an initial financial commitment of only two years. Applicants are free to apply as often as they like and may receive financing for programs targeting the same disease in consecutive Rounds (i.e., they may receive approval for proposals that overlap both in content and chronologically).

6. This model has considerable strengths and has worked remarkably well in launching the Global Fund. It has succeeded in identifying technically strong programs in virtually every eligible country in the world and the first results suggest that the TRP has done a commendable job selecting technically sound proposals. Nonetheless, this approach has some obvious flaws, which are fivefold.

7. First, a rigid proposal process forces applicants to adapt their planning cycles to the Global Fund's, rather than building on pre-existing planning cycles. This adversely impacts attempts to rationalize planning processes under a single national framework and so creates additional work for recipients. Additionally, because the proposal approval occurs on a Global Fund-determined schedule, recipients are also hindered in their ability to incorporate Global Fund resources into annual budgets or Medium-Term Expenditure Frameworks.

8. Second, the use of a standard proposal form militates against the original vision of a Global Fund financing the gaps in a well-mapped landscape of existing efforts, by encouraging applicants to think of Global Fund financing as standalone projects, rather than starting with a pre-existing disease control strategy and simply identifying the financing gaps in it. This can have important negative ramifications for the implementation of Global Fund-financed programs, as it encourages in-country partners to think of the Global Fund financing as a "Global Fund project," rather than as a contribution to scaling up an existing program and therefore something in which all actors have a stake and so need to work to ensure the success of.

9. A project mentality also seems to encourage the submission of smaller proposals, as well as repeated submissions in multiple Rounds (tendencies which may be exacerbated by a publicly-available proposal rejection rate of 60%, which may prompt recipients to hedge their risks by submitting smaller proposals more frequently, knowing that they are not likely to be approved every time). The net effect is to promote smaller proposals that may only partially address the gaps in financing. Given that there is a certain amount of work that is invariable for both the recipient and the Secretariat regardless of the size of a proposal, this increases transaction costs without conferring much benefit.

10. Third, there is an insufficient incentive structure in place to encourage CCMs either to be broadly representative and well-governed, or to harmonize with other actors in the fields of AIDS, tuberculosis and malaria. After a relatively perfunctory screening prior to TRP review, all CCMs are treated equally, with the same proposal review process and identical access to financing, regardless of the quality of the CCM. Given that proposal submission is currently the single most important responsibility of a CCM, the lack of incentives here diminishes the likelihood of CCMs living up to the founding vision of a broadly representative body. Indeed, reviews of their performance clearly suggest that there is considerable room for improvement, in terms of composition, governance, and harmonization.

11. Fourth, the proposal process makes no distinction between programs that focus on life-long or long-term interventions (particularly antiretroviral therapy and the treatment of multi-drug resistant tuberculosis), and those that deal with activities with shorter time horizons (such as the distribution of insecticide-treated nets or condoms). At the moment, both types of interventions are financed in an identical manner, despite the fact that the need for predictability is much greater for the first set of activities than for the second. This absence of predictability may discourage applicants from submitting ambitious treatment-focused proposals.

12. Fifth, there is currently a considerable amount of time between when a proposal is submitted and when its fate is decided upon by the Board of the Global Fund, time that is not systematically used by recipients to prepare for program implementation. In particular, one to two months elapse between when the TRP finalizes its recommendations on the technical

merits of proposals and the convening of the Board, time that could be more productively utilized.

13. There are a range of possible responses to these problems, which can be grouped into those that address a piece of the puzzle, and those that present an integrated response.

14. On the former, the Global Fund could move away from a Round-based approach to instead identifying technically-sound proposals on a continuous basis. Eligible applicants would then be able to submit proposals at times aligned with their existing systems, rather than only in response to the Global Fund's timing. Rather than completing a standard proposal form, applicants could be able to use whatever format they wished, as long as they demonstrated that they had systematically reviewed existing activities and had identified a gap in financing that, when addressed with Global Fund resources, would enable the rapid scale-up of proven interventions against AIDS, tuberculosis and malaria. As a variation to this, applicants could simply submit their national strategic plans for the coming years, with the gaps in financing clearly highlighted. (An ancillary benefit of this approach would be to contribute to the strengthening of the national strategic planning process.) Either of these approaches would facilitate the integration of Global Fund financing with existing systems, such as sector-wide approaches, and with existing planning and budgeting processes, such as Medium-Term Expenditure Frameworks.

15. To reduce transaction costs and encourage scale-up programs that address significant gaps in the financing of disease control strategies, a lower limit to the size of proposals could be instituted (which could be related to a recipient's disease burden and/or population size).

16. An approach to addressing the problem of the lack of incentives for CCMs would begin with the premise that the Global Fund is already active in virtually every eligible country. It would then establish a rating system for CCMs, based on a set of objective criteria (composition, functioning, evidence of harmonization with existing systems, track record in preparing proposals that were deemed technically-sound, etc.) and/or periodic assessments. This would enable CCMs to be grouped into a simple classification system (e.g., A, B, and C).

17. Well-performing CCMs would be rewarded with increased flexibility and/or access to financing. For example, their proposals could be subject to a lighter review by the TRP and could receive priority in the event of resource constraints. If a CCM was unable to meet certain minimum criteria, it could be ineligible to receive any funding at all. The duration of proposal approval could also be ranged according to the quality of a CCM: for example, "A"-rated CCMs could see their proposals approved for ten years and receive five-year commitments at approval, whereas "C"-rated CCMs could only expect to be approved for four years and receive commitment for an initial two years.

18. To ensure that this rating system does not worsen inequality by punishing CCMs in resource-poor settings that are unable to find the financing necessary to support a smoothly running CCM, resources could be made available to CCMs.

19. To avoid a bias against life-long/longer-term treatment interventions, a distinction could be introduced between proposals that target these interventions and those that do not, with the former receiving a commitment of funding (subject to ongoing performance) of five (or more) years, rather than having a check (which is additionally subject to resource constraints) after two years.

20. The time between when the TRP reviews proposals and the Board approves them could be used to allow recipients to respond to the questions that the TRP raises about their proposals (clarifications that now occur after Board approval, delaying the process of signing a grant agreement). This would obviously have to be done in such a way that a recipient is

not misled into thinking that its proposal has been approved by the Board, but such an approach is used in other funding mechanisms, so this challenge is not insurmountable.

21. An integrated solution would start with a rating system for CCMs as outlined above. However, it would take the outcomes of this one step further and provide well-performing CCMs with a block grant for them to draw upon. Once a CCM had demonstrated a track record (and subject to regular performance reviews of both the CCM itself and the implementation arrangements that it had established), it would not need to submit standalone proposals to the Global Fund (or perhaps would only provide a broader disease control strategy), but rather would have access to a multi-year stream of financing. The financing itself would continue to flow directly to PRs, but CCMs would determine the appropriate allocation between multiple PRs.

22. Such an approach would simultaneously create incentives for CCMs to improve, increase predictability, and accelerate the disbursement of funds (by enabling CCMs to focus on supporting implementation, rather than devoting time and energy to proposal submission). This would also enable CCMs to fill gaps in financing their disease control strategies with maximum flexibility, responding to changing conditions and targeting resources to the areas and populations with the most need. Such an approach would considerably ease the challenges of dealing with changing scientific evidence, as CCMs would be able to reprogram resources more easily, without, for example, having to come back to the Global Fund to seek supplemental resources in order to finance a newer, more expensive intervention. It would also contribute significantly to reducing the Secretariat's workload, while preserving the organization's commitment to financing technically-sound interventions (but would shift the locus of determination of the quality of the interventions from the TRP to accredited CCMs).

B. Implementation arrangements

23. Currently, once a proposal has been approved, one or multiple PRs chosen by the CCM are assessed by the LFA to determine whether they have adequate capacity in four domains (financial management and systems, institutional and programmatic arrangements, procurement and supply management, and monitoring and evaluation). These assessments, along with a review of a workplan, budget, and set of indicators based on the approved proposal, form the basis of grant negotiations, ultimately enabling an agreement to be signed between the PR and the Secretariat. A separate grant agreement is signed with each PR for each disease (e.g., if a single proposal focuses on three diseases and is split into two PRs, a total of six agreements would be signed). Separate agreements are also signed even if a PR has an ongoing grant agreement covering the same disease but from a proposal submitted in an earlier Round.

24. Over the duration of the grant agreement, the PR is fully responsible for all aspects of implementation, including disbursing funds to other implementing parties and monitoring programmatic progress. The CCM's role is to provide oversight and technical assistance to this process. Funds are disbursed against the combination of attainment of programmatic results and the demonstration of sound financial practices, a process that typically occurs on a quarterly or semi-annual basis. Towards the end of the second year of program implementation, the CCM submits a request for continued financing, which describes the progress made to date and sets out a vision for the remainder of the original proposal duration that reflects the lessons learned in the first two years of implementation and any changes in circumstances.

25. This process has enabled the Global Fund to rapidly move from approving proposals to disbursing considerable sums in a large number of countries. As can be seen in the results

from the first grants to reach a year of implementation, many recipients have been able to transform this model into successful operational arrangements that enable the rapid scaling-up of responses to the three diseases. Moreover, the approach to performance-based funding seems to be working, as poor performers are generally not receiving ongoing financing, whereas those that meet their targets are rewarded with replenishments.

26. However, this success is not uniform, and three areas have been identified in which structural changes could be beneficial.

27. First, Global Fund financing has already reached nearly every eligible country, meaning that new Rounds will typically result in incremental financing to PRs who have already signed grant agreements with the Global Fund. As the market becomes saturated, the logistics of signing, reporting on, and reviewing the progress of separate grant agreements for the same PR will become progressively more illogical and will create an increasingly daunting volume of transactions. Having separate grant agreements creates diseconomies of scale for PRs, LFAs, and the Secretariat and compounds the problems identified above of Global Fund financing being perceived as standalone projects instead of flowing into existing programs with minimal transaction costs. The need for grant-by-grant reporting will also work against efforts to build a single national monitoring and evaluation system.

28. Second, in an analogous situation to what was described above, there are insufficient incentives in place to ensure that CCMs stay engaged once a proposal is approved. Neither the CCM collectively nor individual CCM members are held accountable for the success of program implementation until the Phase 2 decision-point. At the moment, a CCM could be essentially dormant between the signing of a grant agreement and its request for continued funding for Phase 2. Such a situation would be deleterious both to the speed of program implementation and to the broader attempt to ensure that Global Fund-financed programs are reflective of a genuine partnership approach.

29. Third, the current system appears to be only suboptimally reaching the full range of stakeholders involved in the fight against these three diseases. Currently, approximately two-third of PRs are governmental bodies. In many countries, the government has limited comparative advantage – or even familiarity with – disbursing large sums of money in a rapid manner to myriad small community-based organizations. This lack of capacity is even more pronounced when it comes to disbursing funds to private sector firms and groups of people living with or affected by the three diseases. Further, some governments are restricted by public finance regulations in their ability to pass funding on to private entities except in very limited situations.

30. The first problem – of proliferating grant agreements with a single recipient – could be tackled by consolidating agreements across Rounds, across diseases, or both. For example, instead of signing a distinct new agreement with a PR that already has an active grant for a given disease every time a new proposal is approved for that disease, the new financing could simply be added to the existing agreement, with targets scaled up commensurately. This would create economies of scale, in which all of the work that invariably accompanies the preparation of and reporting on a single grant agreement is rendered unnecessary, considerably reducing transaction costs for both recipients and the Secretariat. This would also move the organization away from focusing on a single grant as the basic unit of work towards a more holistic picture of Global Fund financing to a given recipient.

31. A response to the second challenge, around the lack of incentives for CCMs to be involved in implementation, would be to reserve (each time a proposal is approved) an additional amount to create a fund from which a CCM could pay for technical assistance. The amount would be a function of a combination of the size of the proposal and the quality of the CCM. Building on the rating scheme described above, well-performing CCMs would

have more funds placed at their disposal to finance technical assistance, whereas those that have demonstrated no commitment to broad representation and good governance would not be allocated any funds.

32. Another form of incentive to promote CCM involvement in program implementation would be to weight explicitly performance in ongoing grants in the consideration of new proposals. At the moment, the TRP does factor current performance into the review of new proposals, but this is not done systematically. Moreover, without a clear signal to CCMs that their involvement in ensuring the success of earlier proposals is essential, this informal system is unlikely to create a sufficient incentive for CCMs to engage more proactively in providing assistance to slow-moving programs.

33. A final way to address incentives for CCM performance could dovetail with existing discussions on providing financing to CCMs for meeting and running costs, with the performance of the CCM determining the amount of funding the CCM receives (or, after an initial allotment to all CCMs that need financing, ongoing funding could be tied to performance).

34. The third problem identified above – of designing implementation arrangements that facilitate the rapid disbursement of funds to a wide range of public and private partners – was discussed at great length in the formative early days of the Global Fund. The Framework Document itself contains several relevant ideas that were never operationalized but which should be reexamined in light of the first two years of experience.

35. In particular, the Framework Document describes using two routes or “windows” of financing in a country with an approved proposal. One of these would cater for the public sector, whereas the other would service civil society and the private sector. The former would likely be either the Ministry of Finance or the Ministry of Health, whereas the latter would take a much more country-specific form, depending on the strength of local institutions (for example, a strong umbrella body for non-governmental organizations, or a social investment fund that had demonstrated the ability to rapidly disburse funds to non-governmental entities) and on the nature of the proposal (for example, if a proposal focused on co-investment with a particular private sector firm, this company would be a logical choice).

36. Some CCMs have already chosen to go this route and have selected multiple PRs. As seen in Zambia, this approach facilitates the disbursement of funds to the non-governmental sector. This sort of arrangement could be systematized. A standalone version of this would be to require two PRs for each approved proposal, but not to change other aspects of the architecture.

37. However, combine the idea of having two windows with some of the concepts touched upon earlier, and a vision of a new architecture emerges. There would be two routes of Global Fund financing, one for the public sector, one for the non-public. If governed by a well-performing CCM and if able to demonstrate a strong track record in program implementation, each entity would have access to a multi-year stream of financing, which would be used to finance the range of implementation activities in the respective sectors. Although there might be some concerns about coordination between the two PRs, this apprehension could be transformed into an advantage by locating the responsibility for coordination with the CCM, thus simultaneously developing an important role for CCMs in the course of implementation.

38. Such an approach would be likely to accelerate implementation, both by enabling each sector to concentrate on their areas of comparative advantage, and by removing some of the areas generating considerable transaction costs in the current model. It would

simultaneously strengthen country ownership of the entire process and be easier for the Secretariat to manage.

39. There would likely be some growing pains, as in some countries the non-public sector is fractured and lacks organizations with the strong institutional capacity needed to fulfill the role of such a financing window. Indeed, in some cases, a regional structure might be more appropriate than a purely local one. Further, the cultures and approaches of non-governmental and faith-based organizations and groups of affected communities, on the one hand, and the private sector, on the other, are often radically different, and there are sure to be tensions as they work more closely together.

C. Oversight mechanisms

40. The cornerstone of the Global Fund's approach to overseeing program implementation is the Local Fund Agent. LFAs are typically private sector accounting firms and are contracted directly by the Secretariat.

41. LFAs carry out assessments of the capacity of PRs to handle implementation in four domains, as noted above. In the course of implementation, PRs themselves are responsible for the bulk of monitoring and evaluation activity, but LFAs verify the financial and programmatic reports of PRs, and provide recommendations on them to the Secretariat. The role of the LFA stops with verification and oversight: they do not provide technical assistance to implementers or assist in capacity building, and they do not handle grant proceeds. CCMs have little formal role in ongoing oversight until they are called upon to synthesize progress in their request for Phase 2 financing.

42. While LFAs have succeeded in providing the Global Fund with a considerable degree of reassurance about the accountable use of Global Fund financing, the very concept of the LFA has engendered more speculation and suspicion than any other part of the Global Fund's fiduciary architecture. Much of this skepticism emanates from misunderstandings of the role of the LFA (e.g., questioning why accounting firms would be used to provide technical assistance on programmatic issues, which stems from a misconception that the LFA should be engaged in providing technical assistance). However, two aspects of the current approach are clearly in need of reform.

43. First, the use of accounting firms to handle assessment and verification in domains outside their core competencies has sometimes proven problematic. The original vision was that these firms would possess the requisite experience in contracting outside expertise to fill the gaps in their in-house systems, but this approach has yielded mixed results. Some LFA offices have been able to mobilize the needed skills rapidly and cost-effectively, but in other cases the need for the LFA to contract an independent expert has increased both the time required and the cost of assessments.

44. A second problem with the current structure is that it makes insufficient use of existing systems, including both the CCMs and other, external mechanisms. As noted above, CCMs have little formal role in oversight, despite the fact that their members often have considerable expertise in the area. At the moment, the LFA oversight structure is parallel to other existing systems. For example, if a sector-wide approach is in place, other donors have agreed to use an integrated system for overseeing the use of their funds, whereas the Global Fund still insists upon the use of its LFA. As with the preceding point, this over-reliance upon a uniform LFA approach is both costly and unnecessarily slow.

45. The response to both of these problems could be to move away from a one-size-fits-all concept of an LFA to a tailored approach that is more sensitive to context. This would

maintain the level of fiduciary security provided by the current LFA system, but would do it in a more efficient and cost-effective manner.

46. One part of this would be to unbundle the LFA role, with different firms contracted by the Secretariat based on their comparative advantages. For example, in a grant that contains considerable procurement and supply management, the Secretariat would directly contract a procurement expert or a specialist procurement agency, rather than relying on an accountancy firm to handle this. To oversee a grant that involves a particularly complicated set of health interventions, the Secretariat would use an organization that specializes in the assessment and review of health sector programs, to complement the financial acumen of an accounting firm. The benefits of such an approach would need to be weighed against the increased transaction costs for the Secretariat.

47. A second possible way of addressing the current problems would be to make better use of existing systems. For example, if the Health Metrics Network proceeds with developing an accreditation scheme for monitoring and evaluation systems, the Global Fund could simply buy into the scheme and use its outputs, rather than paying an LFA to redo this assessment, thereby both speeding up the process and saving money. Similarly, if a number of donors have agreed to a sector-wide approach that has established an effective oversight mechanism on expenditure in a given sector, hiring an LFA to play exactly this same role is neither cost-effective nor rapid, so the Global Fund could simply use the existing accountability structures. However, it must be noted that, of the 128 countries in which the Global Fund is operating, fewer than 20 have fully-fledged health sector-wide approaches.

48. A final response to the problems identified would build upon the CCM rating system described above. Highly-rated CCMs – which would have to demonstrate capacity in key areas in addition to being representative and having good governance – would assume some oversight responsibilities. For example, a CCM judged to have strong monitoring and evaluation skills would take the responsibility for carrying out the monitoring and evaluation assessment of the PR. Such a CCM could also take on the responsibility of making recommendations to the Secretariat about the performance of the PR, subject to periodic verifications by the LFA, which would obviously dovetail well with the earlier discussions of the use of block grants. Any moves in this direction would need to be carefully designed to ensure that they would in no way weaken the Global Fund's emphasis on fiduciary responsibility, but doing so could result in a cost-effective way to simultaneously create incentives for CCM performance and take advantage of the fact that there are CCMs that can provide reliable reviews and recommendations.

Part 4: Gaps in the architecture

1. In the course of its regular interactions with recipients and other stakeholders in the fight against the three diseases, the Secretariat is repeatedly asked why the Global Fund is not doing more to address critical bottlenecks to scaling up the responses to AIDS, tuberculosis and malaria. Three topics have been identified by recipients and partners as areas in which the Global Fund is not currently heavily engaged, but in which the organization is ideally situated to contribute meaningfully:

- a. Improving the predictability of supply of critical health products;
- b. Disseminating lessons learned and best practices, facilitated by commitments to operational research; and
- c. Systematizing information on technical assistance.

2. First, the Global Fund is the world's largest financier of a number of health products. This is already true of key malaria-related products, such as artemisinin-based combination

therapy and insecticide-treated nets, and is probably also true of antiretroviral therapy. However, this purchasing power is not being used to ensure the reliable availability of affordably priced products.

3. As a first step, the Global Fund could contribute to improving the predictability of supply of certain key health products by showing to the market the value of the financing available. This could be as simple as establishing separate accounts with the Trustee containing the funding that is expected to be disbursed for key products (as has recently been done for artemisinin-based combination therapy), or could involve establishing an escrow account dedicated to procurement in a commercial bank. Either would signal to producers the expected volume of resources available, in turn enabling them to have more confidence in gearing up production to meet this need.

4. Additionally, such a pool of funds would create an incentive for producers to enter the market, thereby promoting competition. Taking that further, the pool of resources could be leveraged to negotiate price reductions based on the large volumes being procured, or could be used to establish a centralized relationship with a procurement agent to move products to recipients more rapidly than is currently occurring.

5. A second area in which many recipients request further assistance is dissemination of lessons learned and best practices. The Global Fund currently carries out a few activities that provide opportunities for this sort of horizontal collaboration – holding regional meetings, for example – but strengthening and systematizing this is a repeated request of recipients.

6. A further step down this road would be achieved by expanding the role of the Global Fund in ensuring that high quality operational research is conducted in the context of at least some of its grants. At present, the Global Fund encourages recipients to include operational research budget lines in their proposals, but takes no further steps. Previous experience, for example in the context of World Bank health sector lending, suggests that this money will not be well used and that little high quality operational research will be conducted. The Secretariat has been engaged in initial explorations with suitable partners (the Wellcome Trust, the Global Forum for Health Research, the U.S. National Institutes of Health, the UNICEF/UNDP/World Bank/WHO Special Programme for Research and Training in Tropical Diseases [TDR], and others) concerning possible international mechanisms that would ensure that operational research budget lines are used to the best possible effect and that, on a limited basis, opportunities for large-scale rigorous trials are exploited.

7. The third topic is technical assistance. The Global Fund does not and should not provide technical assistance. However, many recipients turn to the Secretariat for information on where they can secure technical assistance. Strong collaboration with technical partners, especially WHO and UNAIDS, means that the Secretariat is usually well-positioned to direct recipients to these organizations. However, there is less information systematically available either about less traditional sources of technical assistance (e.g., the private sector) or about technical assistance to address some of the managerial bottlenecks that recipients are encountering as they scale-up (e.g., financial management systems at peripheral level, procurement and supply management capacity).

8. To respond to the requests of recipients, the Secretariat could continue with the current ad hoc approach, or could develop (or outsource the development of) a more systematized response. For example, this could take the form of a robust information platform that would enable recipients to learn about purveyors of technical assistance, so they could identify an entity well-suited to address their particular challenges. Such a platform could be interactive, with recipients able to connect directly with providers of technical assistance in a virtual brokering service that would optimize the use of Global Fund resources available for technical assistance.

Part 5: Next steps

1. The options for change described above cover a wide array of modifications, with some being only minor adjustments within existing Board policies, and others representing fundamental shifts in the way the Global Fund operates. The Secretariat anticipates receiving guidance and direction from the Board Consultation occurring on 20 November 2004, and stands ready to take the appropriate next steps.