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PERFORMANCE AUDIT REPORT

**CARIBBEAN DEVELOPMENT BANK V
(LOAN 3200, CREDIT 2135)**

**CARIBBEAN DEVELOPMENT BANK VI
(LOAN 3772, CREDIT 2640)**

August 8, 2000

Operations Evaluation Department

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Acronyms

BOAD	West African Development Bank
BMCs	Borrowing Member Countries
CARICOM	Caribbean Community
CDB	Caribbean Development Bank
CDF	Caribbean Development Facility
CGCED	Caribbean Group for Cooperation in Economic Development ¹
EEC	European Economic Community
FRG	Federal Republic of Germany
IDB	Inter-American Development Bank
LDCs	Less Developed Countries
MDB	Multilateral Development Bank
OCR	Ordinary Capital Resources
OECD	Organization for Economic Cooperation and Development
OECS	Organization of Eastern Caribbean States
UNDP	United Nations Development Programme

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Acting Director-General, Operations Evaluation:	Mr. Ruben Lamdany
Acting Director, Operations Evaluation Department:	Mr. Ruben Lamdany
Manager, OEDCR:	Mr. Ruben Lamdany
Task Manager:	Mr. Michael Lav

¹ Antigua and Barbuda, Dominica, Grenada, St. Kitts-Nevis, St. Lucas, St. Vincent and the Grenadines, and Montserrat

August 8, 2000

MEMORANDUM TO THE EXECUTIVE DIRECTORS AND THE PRESIDENT

**SUBJECT: Performance Audit Report on Caribbean Development Bank:
CDB V and CDB VI**

This is a Performance Audit Report (PAR) on the Caribbean Development Bank Fifth and Sixth Projects (Loan 3200 and Credit 2135, and Loan 3772 and Credit 2640, respectively) in the amounts of US\$20 million and SDR 9.1 million, and US\$20 million and SDR 7.8 million. CDB V was approved on January 15, 1990 and closed on December 31, 1997, with a cancellation of US\$13.7 million, and CDB VI was approved on June 29, 1994 and closed on December 31, 1998 with the total loan amount cancelled.

The PAR concentrated on the institutional relationship between CDB and the Bank rather than on the lines of credit in order to focus on the underlying problems which need to be addressed.

CDB V and CDB VI aimed to (a) channel, at a lower cost than the Bank could do directly, additional IDA/IBRD funds to member countries; (b) enhance the amount and scope of development and financial services offered to Bank/CDB borrowing member countries in the Commonwealth Caribbean through better work sharing between the Bank and CDB; and (c) help CDB implement the agreed sectoral and institutional strategies, including its proposed strategy to expand its lending to the private sector through financial intermediaries and for human resources development, and strengthen its institutional capabilities to undertake effective portfolio management and its economic and sector work.

The PAR finds that the outcome of CDB V was unsatisfactory and unlikely to be sustainable, and the outcome of CDB VI was highly unsatisfactory with no rating for sustainability because there were no disbursements. The Institutional Development Impact of both CDB V and CDB VI was Negligible. Borrower performance was unsatisfactory for both, while Bank/IDA performance was unsatisfactory for CDB V and highly unsatisfactory for CDB VI.

CDB V disbursed slowly and a substantial portion was cancelled (US\$8.7 million). The PAR finds that there was virtually no justification for proceeding with CDB VI. For the Bank, an unfortunate short-term focus on new commitments crowded out what should have been a broader institutional focus on building an effective partnership to reduce poverty and improve the living standards of the people of the Caribbean Region. For CDB, the attraction of IDA funds diminished soon after CDB VI was approved as CDB's borrowers' access to grant funds from the European Union and bilateral donors increased substantially.

Beyond this, problems in implementation revealed different perspectives which ought to have been apparent during project appraisal, relating to the faulty incentive structure (involving fixed fees) embedded in the projects, particularly CDB VI. These differences have caused problems in corporate relations beyond the unsatisfactory performance of the projects themselves.

These outcomes are especially problematic given the special role which multilateral subregional organizations such as CDB, and their partnership with the World Bank, ought to play. Therefore, beyond the specific recommendations, the PAR also suggests that the full range of the World Bank's relations with such organizations should be carefully reviewed, to determine if any special procedures or modalities are warranted.

Despite the cancellation of CDB VI at the request of CDB, the Bank's current relationship with CDB involves a number of activities. Co-financing now includes 7 projects, and the Bank and CDB are coordinating with each other on two other projects. The Bank and CDB collaborate in the Caribbean group for Cooperation in Economic Development process, with the World Bank chairing this regional group of countries and donors, and the CDB as a member of the Steering Committee (donor group) and the secretariat for the Committee of Caribbean Member States (country group). The Bank is also working with the CDB in assisting borrowers in the drafting of Medium Term Economic Strategy Papers, especially in the countries of the Organization of Eastern Caribbean States and Belize. Training, including initiatives by the WBI and regional courses, is another important area of collaboration.

Lessons are: (i) Sub-Regional Development Banks like CDB need to be recognized as important partners because of the local expertise and proximity they provide, and the World Bank has a corporate interest in good relations with CDB and other Sub-Regional Development Banks; (ii) as the World Bank collaborates with institutions such as CDB, it needs to devote adequate resources for pursuing collegial remedies to problems. In this process, formal requirements such as deadlines for completion of ICRs should not override the need for full consultation and incorporation of borrower comments; (iii) implementation modalities concerning commitment fees, performance benchmarks, and subloan approval processes should be clearly specified in loan agreements and accessible documents to avoid any possibility of misunderstanding, while fees should be geared to agreed benchmarks rather than fixed by time period.

Robert Picciotto
by Ruben Lamdany

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RATINGS AND RESPONSIBILITIES

	<i>CDB V</i>		<i>CDB VI</i>	
	Evaluation summary	PAR	Evaluation Summary	PAR
Outcome	Unsatisfactory	Unsatisfactory	Highly Unsatisfactory	Highly Unsatisfactory
Sustainability	Uncertain	Unlikely	Not Rated	Not Rated
Institutional Development Impact	Negligible	Negligible	Negligible	Negligible
Borrower Performance	Unsatisfactory	Unsatisfactory	Highly Unsatisfactory	Unsatisfactory
Bank/IDA Performance	Unsatisfactory	Unsatisfactory	Highly Unsatisfactory	Highly Unsatisfactory

KEY STAFF RESPONSIBLE

		<i>Appraisal</i>	<i>Completion</i>
CDBV	Task Manager	Joon Bo Shim	Mariluz Cortes
	Division Chief	Krishna Challa	Max Pulgar-Vidal
	Country Director	Yoshiaki Abe	Orsalia Kalantzopoulos
CDBVI	Task manager	Joon Bo Shim	Mariluz Cortes
	Division Chief	Krishna Challa	Max Pulgar-Vidal
	Country Director	Yoshiaki Abe	Orsalia Kalantzopoulos

ICR'S WERE PREPARED AS FOLLOWS:

CDBV	Loan 3200	Prepared by: Sati Achath
	Credit 2135	
CDBVI	Loan 3772	Prepared by: Sati Achath
	Credit 2640	

Preface

This is a Performance Audit Report (PAR) on the Caribbean Development Bank Fifth and Sixth Projects (Loan 3200 and Credit 2135, and Loan 3772 and Credit 2640, respectively) in the amounts of US\$20 million and SDR 9.1 million, and US\$20 million and SDR 7.8 million. CDB V was approved on January 15, 1990 and closed on December 31, 1997, with a cancellation of US\$13.7 million, and CDB VI was approved on June 29, 1994 and closed on December 31, 1998 with the total loan amount cancelled.

The PAR is based on the joint Implementation Completion Report (ICR) on the two projects prepared by the LAC Regional Office and issued on December 23, 1998, the President's Reports, the legal documents, projects files, related economic and sector work, discussions with Bank staff, CDB staff and documents, and background papers. It focused on the institutional relationship between CDB and the Bank rather than the end use of the lines of credit, since this enables a better focus on the underlying problems which need to be addressed.

An OED mission visited the Caribbean Development Bank and selected borrowing member countries to discuss project performance with CDB staff and officials, and government officials. Their generous cooperation and assistance in preparation of this report is gratefully acknowledged.

The draft PAR was sent to the CDB for comment; the comments received are attached as an Annex to the report.

1. Introduction/Background

1.1 OED selected these two lines of credit to the Caribbean Development Bank (CDB) for evaluation to provide an opportunity to revisit the Bank's institutional relationship with CDB, an important sub-regional partner. This is a priority in light of the unsatisfactory outcomes of the Bank's two last loans to CDB (CDB V and VI) despite the Bank's long-standing relationship with CDB. The focus of the PAR is to examine the causes of the difficult relationship which has emerged between the CDB and the World Bank and to recommend measures which could strengthen this partnership and avoid a recurrence of problems in the future.

1.2 The CDB has the task of promoting economic development and integration in the Commonwealth Caribbean with special regard to the needs of the LDCs in the region. Since its creation, CDB, with substantial assistance from bilateral and multilateral aid agencies (including the Bank), has developed into an important sub-regional development finance institution. The Commonwealth Caribbean governments (particularly those in the Organization of Eastern Caribbean States [OECS]) consider CDB as their own development agency, familiar with local conditions, and want it to play an increasingly important role in the region. From its inception in 1970 through CY98¹ CDB approved loans totaling US\$1.6 billion, of which 56% was for projects in the LDCs. CDB's financial position remains sound with a strong capital structure, high levels of reserves and comfortable liquidity.

1.3 The Commonwealth Caribbean consists of 12 independent countries and five UK dependencies with a total population of 5.7 million people. Based on common interests and heritage, these countries have embarked upon a number of initiatives to construct a framework of cooperation in an attempt to overcome the handicaps of small size, economic fragmentation, and external economic dependence. CDB is one of the most important of these initiatives.

1.4 CDB is one of a small number of sub-regional development banks with which the World Bank has developed a direct lending relationship. This is in contrast to regional development banks such as the Inter-American Development Bank with which the World Bank does not have a direct lending relationship, although it does work closely with them, including cofinancing. Thus, the Bank's relationship with CDB obtains for only a few organizations world-wide (such as the sub-regional bank "BOAD" in West Africa).

1.5 Because sub-regional banks such as CDB have a special relationship with countries in the region, this PAR takes as a starting point that the Bank's relationship with them should be nurtured. This is in line with the Bank's current position vis-à-vis CDB, which comprises a range of technical assistance, parallel lending, and other activities. Recognizing this more explicitly as a priority would justify additional resources to work more closely with CDB, beyond those suggested by normal project coefficients. The resulting institutional partnership would have a large payoff in terms of the welfare of the people of the Caribbean and could, over time, lead to an even more fruitful relationship.

¹ CDB uses the calendar year as its fiscal year.

The Bank's Role in the Commonwealth Caribbean Region

1.6 The Bank has been active in the Commonwealth Caribbean Region since the 1960s, with lending to middle income countries, initially, and then to the CDB in the 1970s which enabled the lower income countries of the OECS to benefit from IDA credits as well as IBRD loans. Parallel with its lending activity, the Bank has undertaken periodic reviews of the Commonwealth Caribbean economies, addressing issues of both country economic performance and broader regional development issues. Until 1984, the Bank's primary focus in the Commonwealth Caribbean was on regional development issues, including the development of subregional institutions. Although some positive results emerged, slower than desired progress led the Bank to subsequently shift to a stronger focus on country policy reforms.

1.7 The Caribbean Group for Cooperation in Economic Development (CGCED) was created in 1977, under chairmanship of the Bank, to channel substantially increased concessionary aid to the Caribbean, to improve aid coordination, and to pursue an enhanced policy dialogue. The CGCED re-affirmed these objectives in 1996 following a comprehensive review of operations, while clearly recognizing that the resource mobilization objective was not as significant.² Within the CGCED framework, the Bank has placed increased emphasis on policy dialogue with the Caribbean aid recipient governments regarding their development priorities and their adoption of sound macroeconomic and sectoral adjustment policies.

1.8 An important recent focus of Bank activity in the Commonwealth Caribbean is the FY99 APL to support disaster recovery and emergency preparedness and management in the OECS countries. This program consists of individual lending operations in the five member countries³ comprising physical investment to protect and strengthen key social and economic infrastructure before disaster strikes, build capacity of national emergency agencies, increase the ability and interest of the private insurance industry to share disaster-related risks, improve and support enforcement of building codes and sound land-use planning, and organize community-level disaster committees and train and equip them to enhance their role in disaster preparedness, mitigation and recovery.

The Bank's Relationship with CDB

1.9 Starting with the administration of the UNDP TA project in 1970, the Bank has sought to support CDB in its growth as a sub-regional development bank. During the 1970s and the 1980s, the CDB evolved progressively toward a full-fledged development bank. Its sound financial management was reflected in a AAA-rating in its first commercial borrowing in 1992. CDB focussed on traditional infrastructure projects during much of this time, in line with the practices at that time of the larger IFIs. The World Bank increasingly relied on CDB to channel funds to the OECS countries, in view

² Text has been modified to take account of CDB's comments. See annexed comments.

³ Dominica, Granada, St. Kitts and Nevis, St. Lucia, St Vincent and the Grenadines. Antigua and Barbuda is also OECS a member state but is not eligible for World Bank lending.

of its lower cost of lending, increasing capacity, and expected similar level of quality. The World Bank also attracted CDB co-financing for some of its projects. The two institutions collaborated in other activities, mainly economic reports and regional papers of the Caribbean Group for Cooperation in Economic Development (CGCED).

1.10 Bank lending to CDB commenced in 1976 and included four projects from 1976 to 1987 for which the Bank lent CDB US\$63 million. CDB I, II, and III were lines of credit, while CDB IV was a US\$6 million credit dedicated to improving education. CDB V and VI, which were both lines of credit, were approved by the Bank in May, 1990, and June, 1994, respectively, and totaled US\$63 million.

1.11 Although the earlier lines of credit were generally satisfactory, CDB V and CDB VI were both non-performing, suffering from slow disbursements. Despite the cancellation of CDB VI at the request of CDB⁴, the Bank's current relationship with CDB involves a number of activities. Co-financing now includes 7 projects⁵, and the Bank and CDB are coordinating with each other on two other projects. The Bank and CDB collaborate in the CGCED process, with the World Bank chairing this regional group of countries and donors, and the CDB as a member of the Steering Committee (donor group) and the secretariat for the Committee of Caribbean Member States (country group). The Bank is also working with the CDB in assisting borrowers in the drafting of Medium Term Economic Strategy Papers, especially in the OECS countries and Belize. Training, including initiatives by the WBI and regional courses, is another important area of collaboration.

2. Objectives

2.1 CDB V and CDB VI aimed to (a) channel, at a lower cost than the Bank could do directly, additional IDA/IBRD funds to member countries; (b) enhance the amount and scope of development and financial services offered to Bank/CDB borrowing member countries in the Commonwealth Caribbean through better work sharing between the Bank and CDB; and (c) help CDB implement the agreed sectoral and institutional strategies, including its proposed strategy to expand its lending to the private sector through financial intermediaries and for human resources development, and strengthen its institutional capabilities to undertake effective portfolio management and its economic and sector work.

⁴ CDB considers that administrative complexities make the World Bank a less attractive source of funding. See annexed comments from CDB.

⁵ OECS Solid Waste Management Project, Emergency Reconstruction and Disaster Mitigation Program (Grenada, St. Kitts and Nevis, and St. Vincent projects); Dominica, Granada and St. Lucia Basic Education Projects; and the planned St. Lucia Water Sector Reform Project. In addition, there is very close collaboration between the Bank's St. Lucia Poverty Fund Project and CDB's St. Lucia Basic Needs Project.

3. Design

3.1 The design of the projects was somewhat complex, but some details are important given the misunderstandings which arose in implementation. CDB V provided US\$20 million in IBRD funds and SDR9.1 million in IDA funds while CDB VI comprised a US\$20 million IBRD loan and a SDR 7.8 million IDA credit as lines of credit to CDB to help finance projects in sectors in which CDB and the Bank had an agreed strategy,⁶ in eligible territories. IBRD and IDA funds were to be blended to finance subprojects.⁷ With IDA funds passed on by CDB at cost, IDA agreed to pay a fixed Administration fee to CDB of US\$660,000 over five years under CDB V and US\$385,000 over five years under CDB VI. CDB was to collect the service charge of 0.75 percent from beneficiary subborrowers and pass it on to IDA. The proceeds of IBRD funds would be onlent by CDB at CDB's interest rate under CDB's "Ordinary Capital Resources (OCR) Financial Policies and Guidelines", with foreign exchange risks to be borne by CDB's subborrowers or governments. To have access to funds, member governments were required to provide guarantees,⁸ as required under the Bank's Articles of Agreement. A guarantee, satisfactory to the Bank, from each eligible country, was a condition of first disbursement of the subloans in each country.

3.2 Two financing issues arose out of the implementation of these arrangements. The first concerns the trigger for incurring commitment fees. In previous lines of credit to CDB there had been prolonged delays in obtaining the country guarantees, and there were considerable delays in the commitment and disbursement of funds. CDB had followed a practice of informally submitting a subproject to the Bank, then proceeding to process it through Board approval, and then, at a later date, formally submitting the subproject to the Bank for approval after which commitment fees would be charged. This trigger for incurring commitment fees was stipulated in the minutes of negotiations and in the IDA credit agreements.⁹ CDB regarded its practices (as did staff which had been supervising CDB V and CDB VI) as a legitimate cost containment measure practiced in a collegial setting. In contrast, the practice was interpreted by the new LAC management following the reorganization of 1997 as inappropriately depriving the World Bank of commitment fees. This difference of views further strained relations.

⁶ These sectors included: agriculture, manufacturing, tourism, transportation, water and sewerage, power, housing and emergency recovery lending. Although private sector development was a priority for both the CDB and the Bank, it was not included because of differences in approach between the CDB and the Bank.

⁷ For CDB V, the blending of IBRD/IDA funds was at a ratio not softer than 50/50 of IBRD/IDA for national projects and 33/67 for regional projects. For CDB VI, loans to countries of the Organization of Eastern Caribbean States (OECS) were to be a 50/50 blend of IDA/IBRD funds for both national and regional projects.

⁸ CDB has commented that the requirement for separate country guarantees as a condition precedent of subloans in each country was a major cause of delay in implementation. It also effectively prevented resources from being channeled to the private sector because of the unwillingness of governments to guarantee private sector borrowing. CDB also noted that because CDB's callable capital is used to "back" CDB's borrowings, a World Bank loan benefits from two guarantees-clearly a redundancy exists. For the full text of CDB's comments, see annex.

⁹ The text of this paragraph was modified to take account of CDB's comments (see annex).

3.3 Second, the fixed fee arrangement was fully agreed by the CDB and the World Bank. However, in the absence of progress in generating subprojects under CDB VI for the first years of CDB VI, the new management of LAC thought that these funds were not being wisely spent, even though the time elapsed was only a portion of the projected life of CDB VI as agreed at appraisal and Board Approval. A deadline was agreed for submitting at least two subprojects to the Bank. When the Bank identified problems with these subprojects (see para. 4.2 below), CDB requested termination of CDB VI before any disbursements had taken place.

Quality at Entry

3.4 Both CDB V and CDB VI suffered from shortcomings in quality at entry. The paragraphs above discuss a series of misunderstandings in key areas which were essential to the operation of the projects. The institutional objectives by which CDB was later judged in the ICR were not tied down in the projects to specific capacity-enhancing investment features which could have been supported by technical assistance and other activities. Nor was there a clear understanding between the Bank and CDB of the operations to be pursued under the lines of credit. Under the fixed fee arrangement, CDB had no financial incentive to use Bank/IDA funds quickly.

4. Implementation

4.1 By the end of 1994, CDB V had been fully committed to six subprojects: St Lucia Road Improvement and Maintenance, Barbados Roads, St Kitts and Nevis Roads, Dominica Sea Defense, Guyana Sea Defense, and Nevis Port Development. However, in mid-1995, the Dominica Sea Defense subproject was cancelled at the borrowers request, because it felt it could not meet its portion of project costs. It was replaced by a new subloan, to finance the Grenada Road Improvement and Maintenance Project. All six subprojects experienced some delays in implementation but five have now been completed (Guyana Sea Defense is the exception). The projects are rated by CDB as of average quality, using a methodology which had been proposed earlier by Bank staff. Supervision costs to the World Bank for the five subprojects came to about US\$31,000 per subproject per year, comprising US\$200,000 of supervision of CDBV and US\$660,000 in Administrative Fees over 5½ years. This compares with an average supervision expenditure of US\$74,000 per project in the Bank's portfolio in the Caribbean Region during 1998. While these sub-projects may be smaller on average than the typical World Bank project in the Caribbean Region, there is no obvious correlation between supervision expenditure and project size below a minimum among very small projects. Finally, there were also considerable savings to the World Bank in terms of subproject preparation and appraisal. CDB V preparation and appraisal cost the Bank less than \$100,000, considerably less than it would have cost the World Bank to prepare and appraise the five sub-projects.

4.2 CDB VI, by contrast, never got off the ground. Two sub-projects were identified (Trinidad and Tobago Roads and Dominica water supply) and given at least informal concurrence by Bank staff. Following its understanding of procedures, CDB intended to

submit the sub-projects to the Bank formally when disbursements began. At this time the Bank staff member supervising CDB VI had been a prior employee of CDB. However, following a change in management in LAC region, the subprojects received another evaluation, based on materials requested at that time from CDB by fax and mail¹⁰ (Some World Bank files regarding the Trinidad and Tobago Roads subproject could not be located). There was a dispute between the Bank and the CDB about whether these evaluations were based on formal or informal requests and other aspects. It was at this juncture that intensive consultations between the Bank and CDB would have been desirable to find a common basis for proceeding. LAC staff concerned with CDB point to budget and staff constraints which prevented such consultations and an adequate airing of the problems and search for an acceptable solution. They also point to pressures to rapidly improve the quality of the portfolio. In the event, the subprojects were simply found wanting by the Bank. Since CDB's Board had approved the subprojects by this time assuming World Bank financing, CDB proceeded to restructure them and finance them without recourse to World Bank funding. CDB then requested cancellation of CDB VI, which was so done without any disbursements having been made.

4.3 Further misunderstandings then occurred regarding possible World Bank assistance for CDB's Strategic Plan and in the course of preparation and distribution of the Bank's Implementation Completion Report for CDB V and VI. In particular, CDB was not able to adequately contribute to the ICR in the time frame defined by the World Bank according to its normal procedures.¹¹ Corporate relations between the CDB and the Bank suffered, although there are several new joint activities, including technical assistance and parallel financing of projects. In addition, relations between working level staff at the CDB and Bank are excellent.

5. Outcomes

5.1 This Performance Audit Report (PAR) agrees with OED's evaluation summaries, finding that the outcome of CDBV was unsatisfactory and unlikely to be sustainable; while the outcome of CDBVI was highly unsatisfactory with no rating for sustainability because there were no disbursements. This assessment is fully in line with the joint ICR and OED's evaluation summaries for these projects. CDBV disbursed slowly and a substantial portion was cancelled (US\$8.7 million). The PAR finds that there was virtually no justification for proceeding with CDB VI. For the Bank, an unfortunate short-term focus on new commitments crowded out what should have been a broader institutional focus on building an effective partnership to reduce poverty and improve the living standards of the people of the Caribbean Region. For CDB, the attraction of IDA funds diminished soon after CDB VI was approved as CDB's borrowers' access to grant funds from the European Union and bilateral donors increased substantially.

5.2 Beyond this, problems in implementation revealed different perspectives which ought to have been apparent during project appraisal, relating to the faulty incentive

¹⁰ Text has been modified to take account of CDB's comments. See annex.

¹¹ This was especially problematic because CDB considered the ICR as lacking in objectivity among other shortcomings. See annexed comments from CDB for more details.

structure embedded in the projects, particularly CDB VI (see paragraph 8.1 below). These differences have caused problems in corporate relations beyond the unsatisfactory performance of the projects themselves.

5.3 These outcomes are especially problematic given the special role which multilateral subregional organizations such as CDB, and their partnership with the World Bank, ought to play. Therefore, going beyond the specific recommendations made in this PAR, the PAR also suggests that the full range of the World Bank's relations with such organizations should be carefully reviewed, to determine if any special procedures or modalities are warranted.

6. Institutional Development

6.1 This PAR rates institutional development in both CDB V and CDB VI as negligible, while the ICR rates Institutional development in CDB V as partial and CDB VI as negligible. However, the ICR discusses various aspects of CDB's "institutional performance" (and finds them wanting), rather than the impact of the project on institutional development. Given the lack of specific objectives regarding institutional development, the lack of supervision guidance in this area as recorded in supervision reports, and the lack of activities and funding devoted to institutional development, a rating of negligible seems most appropriate for both CDB V and CDB VI, which is consistent with OED's evaluation summaries.

7. Sustainability

7.1 Although CDB V achieved little at an institutional level, the subprojects being implemented clearly have some benefits, based on supervision information provided to OED by CDB. However, information available does not provide for a definitive evaluation of the subprojects. In view of this, the PAR rates sustainability for CDB V as unlikely. The ES and the ICR both gave CDB V a rating for sustainability of uncertain, but the rating system has changed and this is rating is no longer available. (The rating system now comprises highly likely, likely, unlikely, and highly unlikely.) Because CDB VI was cancelled in its entirety, it is not rated for sustainability.

8. Bank Performance

8.1 **Bank Performance** is rated as unsatisfactory for CDBV and highly unsatisfactory for CDBVI. The project designs were inadequate, having failed to draw lessons from past projects. Bank supervision reports concerning CDB V were generally positive for years after project approval, and did not adequately identify emerging problems. The first supervision report for CDB V to highlight shortcomings in CDB as an institution was the eighth report issued in February 1998. The prior seven reports, the first of which was issued in April, 1991, did not highlight such shortcomings. The Bank's performance in preparation, appraisal, and implementation of CDB VI fell short of what was needed, again failing to incorporate lessons learned despite the recent problems with CDB V.

Nevertheless, the Bank continued to rate CDB VI performance as satisfactory through 1997 (that is, during the first three years of the project) for some time despite indications of slower than expected progress in lending and institutional reform. The project design features under which the Bank offered the CDB a fixed fee gave CDB no incentive to use Bank funds ahead of other funds. With this arrangement, it could have been expected that CDB, in managing its finances prudently, would use Bank funds largely when other funding was not available, although considerations of partnership could have suggested otherwise. This arrangement simply placed CDB in a difficult position. Finally, the Bank should have been more engaging in dialogue concerning CDB VI, especially concerning the preparation of subprojects, although efforts were made to pursue joint medium-term objectives as reflected in a number of Memoranda of Understanding signed between the two institutions

8.2 CDB's role and performance as a development bank had become an important issue for the Bank. However, the PAR finds that the institution-building aspect of CDB V and CDB VI, and, indeed, previous loans to CDB, were inadequately formulated, although the Bank did make some efforts in this direction in late 1997 and early 1998.¹² While there was a general assumption in CDB V and CDB VI of improved performance by CDB, the projects contained no specific components dedicated to this objective, nor were performance indicators developed. Since the joint ICR for CDB V and VI focused *ex post* on an evaluation of CDB as well as the performance of CDB V and CDB VI *per se*, the lack of agreed *ex ante* performance indicators was especially problematic.

8.3 After the Bank's reorganization in 1997, addressing the poor performance of the LAC Region's Caribbean Department's portfolio became a high priority. CDB V and CDB VI were only two of a number of projects in which problems had emerged, as about two-thirds of the department's portfolio comprised projects at risk. In moving to rapidly clean up the portfolio, in line with the Bank's corporate priorities, it was difficult to arrange for extensive consultations on CDB V and CDB VI (see also para. 4.2). While attempts at dialogue continued at senior levels, there was a lack of communication at the working level regarding processing of subprojects. Some misunderstandings arose regarding procedures, the availability and transmission of information, and other matters. As discussed under Implementation (see paragraph 4.2), these led to CDB itself requested the termination of CDB VI. Further, the Bank adhered to a formal deadline in processing the joint ICR, and after a number of communications, prepared to issue the ICR as deadlines passed but without receiving the concurrence of CDB. The PAR finds that an exception could have been made for CDB in terms of the processing of the ICR, to facilitate more participation, given CDB's special role as a sub-regional borrower, the overlapping membership of the Bank's and CDB's Boards of Executive Directors (so that documentation such as an ICR distributed to the Bank's Board is *de facto* available to much of the membership of the Board of CDB) and CDB's past relationship with the Bank. This would have allowed for a more collegial exchange of views during a difficult time in the institutions' relations, and could have paved the way for a more collaborative approach to addressing the Region's problems. The immediate cost of this approach, a more slowly improving departmental portfolio, might have been offset by a stronger

¹² CDB has a different perspective on what would constitute appropriate institution building and did not consider these efforts as such. See CDB's annexed comments.

partnership with CDB over time, and more efficient and effective support to poverty reduction efforts in the Caribbean.

8.4 Supervision of CDB V and CDB VI had been, under the prior LAC management, the responsibility of a former staff member of CDB. With the reorganization in LAC, this staff member did not have as much credibility with the new management because of this past association, although there is no suggestion whatever that it influenced the individual concerned. Despite years of close collaboration, and without any hint of improper conduct, this may have limited the scope for improving performance.¹³

9. Borrower Performance

9.1 **Borrower Performance** is rated unsatisfactory for both CDBV and CDBVI. However, to the extent that CDB was guided, as it might reasonably have been, by World Bank supervision through almost all of CDB V and much of CDBVI (during which time these reports stated that there were no major problems with CDB), then responsibility for this performance rests both with the World Bank and CDB. Through this time, CDB did strengthen its operational capacity in key areas and maintained a strong financial position. CDB might also have reasonably expected that World Bank standards were an adequate guide to project implementation. By the time the World Bank supervision reports began to note substantial implementation problems, CDB was faced with both a downturn in the economies of the Commonwealth Caribbean, as well as provision of concessional lending to CDB and a sharp increase in grants made available by other donors, especially the European Union, in borrowing member countries which, in turn, diminished the demand for CDB lending and utilization of World Bank funds.

9.2 Slow disbursements were a disappointing aspect of both operations. However, the fixed fee which the Bank agreed to pay CDB and the delays in charging commitment fees meant that there was no incentive for CDB to use Bank funds quickly (see paragraph 3.2 for a more complete discussion). While this PAR finds CDB's performance lacking, much of the fault of slow disbursement can be traced if only indirectly to flaws in project design which the Bank, with its wider experience, should have foreseen more clearly.

9.3 CDB recognizes the need to improve performance and is formulating a Strategic Plan to position itself to more effectively address the needs of the countries of the Caribbean. As part of this evaluation, CDB is expected to continue strengthening its capacity in areas such as social sector projects and the environment with the view that increased support of borrowing member countries in this area would make CDB even more relevant in the future. CDB already has valuable staff and institutional resources. It maintains a strong financial standing and has successfully floated bonds in international capital markets. CDB also maintains a special role as the regional multilateral financial institution for the Caribbean, and has close working relations with the countries of the Caribbean. In these circumstances, the Bank's relations with CDB warrant a larger investment in institutional relations and development to address the issues which arose in

¹³ CDB does not agree with this observation. See CDB's annexed comments.

the context of CDB VI, with a view to building a more effective partnership to pursue regional development priorities over the longer term. All of these factors could bode well for the future relationship between CDB and the World Bank.

10. Findings and Lessons

10.1 The underlying premise guiding the PAR's recommendations is that Sub-Regional Development Banks like CDB need to be recognized as important partners. They provide local expertise and proximity to address development issues. The World Bank has a corporate interest in good relations with CDB and other Sub-Regional Development Banks. A number of recommendations based on this premise and the lessons deriving from the audit of CDB V and CDB VI are given below.

10.2 *Recommendation:* As the Bank addresses portfolio issues, it needs to devote adequate resources to pursuing collegial remedies. This may well involve additional staff and budget resources, and the attention of senior managers, to fully understand and to bring along key partners, especially when changes are sought in long-established procedures and relationships, and where operations have been given satisfactory ratings for long periods of time. It may be that the more rapidly the Bank seeks change, the greater would be the additional staff and budget resources needed to explain such changes and work through them with the Bank's partners.

10.3 *Recommendation:* Performance indicators should be agreed and specified as part of the loan package. Careful thought needs to be given to the most effective way to proceed with such efforts in a collegial manner in the case of a multilateral institution such as CDB. Substantive indicators which address the key performance aspects would be most appropriate, and could be selected from portfolio quality indicators, financial status indicators, and institutional reform indicators included in CDB's strategic compact, but tailored to objectives supported by the World Bank

10.4 *Recommendation:* Deadlines for completed ICRs should not override the need for full consultation and incorporation of borrower comments. This is especially important in sensitive cases such as a subregional development bank like the CDB, with membership of its Board of Directors overlapping that of the Bank's Board of Directors. Indeed, more generally, deadlines concerning corporate relations between the CDB and the World Bank should be defined in terms of reasonable development needs rather than internal bureaucratic imperatives, while acknowledging that corporate standards affecting the quality of operations need to be upheld.

10.5 *Recommendation:* For the future, to avoid even the perception of a problem, staff should not be engaged in supervising World Bank lending to an agency in which they were formerly employed, unless truly exceptional circumstances obtain.

10.6 *Recommendation:* Triggers determining the time at which commitment fees will begin to accrue should be unambiguously agreed and stated in the loan documents.

10.7 Recommendation: Fee arrangements in future loans should be geared to agreed performance benchmarks, rather than the fixed fee arrangements contained in CDB V and VI. If improved operations are defined as part of the objectives of a loan, then a well-defined program of technical assistance could be financed, but should be kept separate from fees which are defined to offset the costs of generating subloans.

10.8 Recommendation: Procedures should be agreed that eliminate the scope for the Bank to reverse a decision concerning subprojects. There should not be any informal subproject approval procedures. The World Bank should have only one opportunity to review subloans and express no objection.

Basic Data Sheet

Fifth Caribbean Development Bank Project Loan 3200, Credit 2135

Key Project Data (amounts in US\$ million)

	<i>Appraisal estimate</i>	<i>Actual or current estimate</i>	<i>Actual as % of appraisal estimate</i>
Total project costs	102.00	N.A.	N.A.
Loan amount	20.0	16.2	81.0
Credit	12.0	7.1	59.0
CDB	28.0	12.0	N.A.
CDB-Co-financiers	18.0	N.A.	N.A.
Sub-borrowers	24.0	N.A.	N.A.
Project completion	6/30/97	6/30/98	
Economic Rates of Return	6-50%	N.A.	N.A.
(weighted average)	21.2%		

Cumulative Estimated and Actual Disbursements

	<i>FY91</i>	<i>FY92</i>	<i>FY93</i>	<i>FY94</i>	<i>FY95</i>	<i>FY96</i>	<i>FY97</i>	<i>FY98</i>
Appraisal estimate (US\$M)	0.6	3.2	8.2	16.0	23.0	28.2	31.2	32.0
Actual (US\$M)	0	0	0.8	4.5	10.3	11.0	14.4	18.3
Actual cumulative as % of Appraisal	0	0	10.0	27.9	44.9	38.9	46.2	57.2

Date of Final Disbursement: September 24, 1998

Project Dates

	<i>Original</i>	<i>Actual</i>
Identification/Preparation	April 1989	June/July 1989
Appraisal	June 1989	December 1989
Negotiations	NA	March 1990
Board Approval	January 15, 1990	May 22, 1990
Signing	NA	June 18, 1990
Effectiveness	NA	September 6, 1990
Loan Closing	December 31, 1997	December 31, 1998

Staff Inputs (staff weeks)

Stage of Project Cycle	Actual
	Weeks
Preparation to Appraisal	43.7
Appraisal	2.5
Negotiations through Board Approval	39.7
Supervision	53.1
Completion	5.1
Total	144.1

Mission Data

Stage of project cycle	Date (mm/yr.)	No. of persons	Duration of mission (# of days)	Specialized staff skills represented	Performance rating		Types of problems
					Implement. status	Develop. objectives	
<u>Through Appraisal</u>							
1. Identification/Pre-appraisal	June/ July 1989	3	20	Task/Mgmt. Operations			
2. Appraisal/Post-appraisal	Dec. '89	NA	10	Task/Mgmt. Operations			
<u>Appraisal through Board Approval</u>							
Supervision							
Supervision 1	April 1991	1	7	Task/Mgmt. Operations	NA	1	No major problems
Supervision 2	July '92	2	5	Task Mgmt/ Operations/ Finance	NA	1	Increase in arrears
Supervision 3	May '93	3	10	Task Management	NA		No major problems
Supervision 4	July '94	1	NA	Task Management	S	S	Slow disbursement
Supervision 5	May '95	1	NA	Task Management/ Legal	U	S	Slow disbursement
Supervision 6	June '97	1	5	Task Management	U	S	Weak implementation capacity in member countries, slow disbursement
Supervision 7	Dec. '97	2	2	Task management	U	S	Implementation delays due to fiscal shortages, labor unrest, natural disaster, etc.
Supervision 8	Feb. '98	2	6	Task Management/ Priv. Sector Dev.	U	U	CDB's low quality of project work, human resource constraints, low utilization of funds

Other Project Data

Borrower: Caribbean Development Bank

Related Bank Credits

Loan/Credit title	Purpose	Year of approval	Status
Preceding operations			
First Caribbean Dev. Bank Project	To help develop CDB as an institution and as a channel for indirect Bank lending to the Commonwealth Caribbean	1976	Closed (1982)
Second Caribbean Dev. Bank Project	To help develop CDB as an institution and as a channel for indirect lending to the Commonwealth Caribbean	1979	Closed (1986)
Third Caribbean Dev. Bank Project	To help develop CDB as an institution and as a channel for indirect Bank lending to the Eastern Caribbean countries	1983	Closed (1992)
Fourth Caribbean Dev. Bank Project (Regional Vocational and Technical Education Project)	To improve the quality and quantity of trained manpower in the OECS states	1987	Closed (1994)

Following Operations

Sixth Caribbean Dev. Bank Project	To help develop CDB and as an institution and as a channel for indirect Bank lending to the Commonwealth Caribbean; enhance the scope of development and financial services to member countries; and help CDB expand its lending to private sector, and for human resources development	1994	Cancelled
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Basic Data Sheet

Sixth Caribbean Development Bank Project Loan 3772, Credit 2640

Key Project Data (amounts in US\$ million)

	<i>Appraisal estimate</i>	<i>Actual or current estimate</i>	<i>Actual as % of appraisal estimate</i>
Total project costs	68.0	0	0
IBRD/IDA	31.0	0	0
CDB	17.0	0	0
CDB-cofinance	8.0	0	0
Sub-borrowers	12.0	0	0
Date physical components completed:		Not applicable	
Economic rate of return		Not applicable	

Cumulative Estimated and Actual Disbursements

	<i>FY96</i>	<i>FY97</i>	<i>FY98</i>	<i>FY99</i>	<i>FY2000</i>	<i>FY2001</i>	<i>FY2002</i>
Appraisal estimate (US\$M)	0.5	2.1	5.5	13.5	25.0	29.2	31.0
Actual cumulative as % of Credit	There was no disbursement at all						

Project Dates

	<i>Original</i>	<i>Actual</i>
Identification/Preparation	NA	May/June 1993
Appraisal	October 1993	Nov./Dec. 1993
Board Approval	NA	June 29, 1994
Signing	NA	Oct. 4, 1994
Effectiveness	NA	July 27, 1995
Project Completion	June 30, 2002	Not applicable
Loan Closing	December 31, 2002	Cancelled May 25, 1998

Staff Inputs (staff weeks)

Stage of Project Cycle	<i>Actual</i>
	<i>Weeks</i>
Preparation to Appraisal	13.5
Appraisal - Negotiation	6.7
Negotiations through Board Approval	18.1
Supervision ^a	36.8
Completion	11.0
Total	86.1

Mission Data

Stage of project cycle	Date (mm/yr.)	No. of persons	Duration of mission (# of days)	Specialized staff skills represented*	Performance rating		Types of problems
					Implement. Status	Develop. objectives	
<u>Through appraisal</u>							
1. Identification/ preappraisal	May/June 1989	2	14	Task Mgmt/ Finance			
2. Appraisal	Nov.- Dec. '93	2	12	Task Mgmt/ Finance			
Appraisal through Board Approval					-	-	-
<u>Supervision</u>							
Supervision 1	Feb. 96	1	NA	Task Mgmt/ Finance	S	S	No major problems
Supervision 2	Dec. 96	1	NA	Task Mgmt/ Finance	S	S	No major problems
Supervision 3	June 97	1	5	Task Mgmt.	U	S	Weak implementing capacity in member countries, slow disbursement
Supervision 4	Dec. 97	1	2	Task Mgmt.	U	S	Delays due to fiscal shortages, labor unrest, natural disaster, etc.
Supervision 5 ¹⁴	Feb. 98	2	6	Task/Mgmt Operations/ Private Sector Development	U	U	CDB's low quality of project work, human resource constraints, low utilization of funds.

¹⁴ Received QAG's 'Recognition of good Supervision performance' commendation

Other Project Data

Borrower: Caribbean Development Bank

Related Bank Credits

Loan/Credit title	Purpose	Year of approval	Status
Preceding operations			
First Caribbean Dev. Bank Project	To help develop CDB as an institution and as a channel for indirect Bank lending to the Commonwealth Caribbean	1976	Closed (1982)
Second Caribbean Dev. Bank Project	To help develop CDB as an institution and as a channel for indirect lending to the Commonwealth Caribbean	1979	Closed (1986)
Third Caribbean Dev. Bank Project	To help develop CDB as an institution and as a channel for indirect Bank lending to the Eastern Caribbean countries	1983	Closed (1992)
Fourth Caribbean Dev. Bank Project (Regional Vocational and Technical Education Project)	To improve the quality and quantity of trained manpower in the OECS states	1987	Closed (1994)
Fifth Caribbean Dev. Bank Project	To help develop CDB as an institution and as a channel for indirect Bank lending to the Commonwealth Caribbean; and enhance the scope of development and financial services to member countries	1990	Closed (1998)

Following Operations

Sixth Caribbean Dev. Bank Project	To help develop CDB and as an institution and as a channel for indirect Bank lending to the Commonwealth Caribbean; enhance the scope of development and financial services to member countries; and help CDB expand its lending to private sector, and for human resources development	1994	Cancelled
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**CARIBBEAN
DEVELOPMENT
BANK**

P.O. Box 408, Wildey, St. Michael, Barbados, W.I.
Telephone: (246) 431-1600 (PABX)
(246) 431-1890 (Direct)
Telefax: (246) 228-9670 / Telex: WB 2287
Cable Address: "Caribank" Barbados
Website: www.caribank.org

PRESIDENT

July 17, 2000

Mr. Reuben Lamdany
Manager
Country Evaluations and Regional Relations
Operations Evaluation Department
The World Bank
1818 H Street, NW
Washington, DC
UNITED STATES OF AMERICA

Dear Mr. Lamdany:

**Performance Audit report
CDB V (Loan 3200, Credit 2135)
CDB VI (Loan 3722, Credit 2640)**

Please find enclosed the Caribbean Development Bank's comments on the referenced Performance Audit Report.

In general, we find the Report to be well balanced. In our view, it would go a long way toward reinforcing the long-standing relationship between our two institutions. The fact that the preparation of the report included an actual visit to the Bank and Borrowing Member Countries, no doubt, facilitated depth of insight that the reviewer obtained. This significantly contributed to the quality of the Report.

Yours sincerely,

A handwritten signature in dark ink, appearing to read "Neville V. Nicholls".

Neville V. Nicholls
President

CARIBBEAN DEVELOPMENT BANK

Comments on Performance Audit Report

CDB V (Loan 3200, Credit 2135)

CDB VI (Loan 3722, Credit 2640)

General

The Performance Audit Report (PAR) is a well-balanced study. It correctly deals with the issues from the institutional relationship perspective rather than attempting to analyse the end use of the credit lines. At the same time, since the PAR was based, *inter alia*, on the Implementation Completion Report¹ (ICR), the issues raised in the ICR together with CDB's comments, should have been more directly addressed. This is particularly so since the PAR acknowledges that the non-incorporation of CDB's comments in the ICR, essentially for bureaucratic reasons, contributed to a deterioration of the relationship between the two institutions.

CDB considered the ICR itself as containing several inaccuracies and baseless criticisms. Quoted below is an extract from CDB's comments, which gives a fairly clear idea of CDB's view of the ICR:

"The World Bank ICR lacks objectivity in many areas that are discussed below. The links between facts, analysis and conclusions are often absent and cast doubt on both the thoroughness of the work and the fairness of the judgments applied. The choice of adjectives and phrases compound the problem and result in a generally unfair critique not based on the facts. The tenor of the report is such that one is forced to question the motives underlying its preparation. The consultant who prepared the report did not engage in dialogue with the CDB."

CDB highly values its relationship with the World Bank. This is clearly evidenced by the number of co-financing activities currently operating and our involvement with the CGCED. It is doubtful, however, that it would be in CDB's interest to seek to obtain funding from the World Bank in the future. The administrative complexity involved in operating a World Bank loan is such that other sources of funding are likely to be preferred - that is, unless the World Bank is prepared to be flexible and utilize a more appropriate modality. But the PAR does not address this issue.

¹ World Bank Report No. 18738. This included CDB's own contribution at Appendix B.

Specific

1. **Paragraph 1.7 (page 2):** It may be useful to note that the original objectives of the CGCED were: (i) Resource Mobilisation (ii) Aid Coordination and (iii) Policy Dialogue. The CGCED re-affirmed these objectives in 1996 following a comprehensive review of the operations, while clearly recognizing that the resource mobilization objective was not as significant.
2. **Paragraph 3.1 (page 3):** The requirement for separate country guarantees as a condition precedent for sub-loans in each eligible country was a major cause of delay in implementation. It also effectively prevented the resources from being channeled to the private sector because of the unwillingness of governments to guarantee private sector borrowing. This was a feature of previous World Bank loans to CDB. The World Bank itself, in a 1986 OED Report on CDB 1, indicated that the separate guarantee requirement "tends to dilute substantially the actual and potential benefits that could be derived from intermediation." It should also be noted that CDB's callable capital is used to "back" CDB's borrowings, so that a World Bank loan benefits from two guarantees – clearly a redundancy exists.
3. **Paragraph 3.2 (page 4):** It is difficult to understand why the formulation of the process in Bank documents was deemed unclear. The formula for charging commitment fees was clearly established in the CDB 6 loan agreement – in Section 2.04 and Section 3.02 of the General Provisions, which were modified by Paragraph 2 of Schedule 7. The modification referred to is quoted below for ease of reference:

"3.02. Commitment Charge. The borrower shall pay a commitment charge on the unwithdrawn amount of the Loan at the rate specified in the Loan Agreement. Such commitment charge shall accrue in respect of each portion of the Loan allocated to a specific IBRD Sub-loan: (i) from the date on which the Bank has notified the Borrower that the Bank has authorized withdrawals from the Loan Account in respect of the IBRD Sub-loan in question pursuant to sub-paragraph (b) of paragraph 3 of schedule 1 to CDB Sixth Development Credit Agreement; or (ii) a date sixty days after the date of the Loan Agreement, whichever comes later (such later date hereinafter called the Accrual Date), to the respective dates on which amounts of the aforesaid portion of the proceeds of the Loan allocated to the IBRD Sub-loan in question shall be withdrawn by the Borrower from the Loan Account of shall be cancelled."
4. **Paragraph 4.2 (page 5):** The meaning of the statement "...the subprojects received another evaluation, based on the strategy for those sectors as agreed between CDB and the World Bank..." is not clear.

Sector strategies were agreed at the time of appraisal of CDB 6 and one can only assume that prior evaluations of the subject projects by the World Bank were also based on those strategies. Yet the evaluations were different. Also, at least with respect to the Southern Roads Project in Trinidad & Tobago, it is difficult to reconcile that the project was only given informal concurrence by the Bank with the fact that the World Bank signed a guarantee agreement with the Government of Trinidad & Tobago on 1st February, 1996 in order to enable CDB to disburse funds to the project. In this context, it is troubling to note that some World Bank files regarding the Trinidad & Tobago Roads subproject could not be located.

5. **Paragraph 8.2 (page 8):** CDB is not aware of any institution-building efforts by the World Bank in late 1997 and early 1998.
6. **Paragraph 8.4 (page 8):** The former staff member of CDB referred to in fact worked with the CDB more than 25 years ago. It is extremely difficult to understand why this should have affected his credibility with the new management because of his past association. More specifically, CDB's own experience when working with the staff member in question indicated a highly professional officer who never compromised his own very high standards. Indeed, all members of CDB's senior management have nothing but respect for the individual. To suggest that his previous association with CDB (25 years ago) "limited the scope for improving performance" is not based on any objective analysis. Further, someone who had no prior relationship with CDB previously supervised CDB V. Yet the two supervisors evaluated performance in the same manner. This would suggest that the past relationship could not have been a factor.