

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

**PERU**

**PROGRAM TO IMPROVE THE QUALITY OF PUBLIC  
MANAGEMENT AND EXPENDITURE II**

**(PE-L1017)**

**LOAN PROPOSAL**

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## ANNEXES

### Annex I            Triggers for 2007

#### Proposed resolution

Electronic Links and References	
Basic socioeconomic data	<a href="http://www.iadb.org/RES/index.cfm?fuseaction=externallinks.countrydata">http://www.iadb.org/RES/index.cfm?fuseaction=externallinks.countrydata</a>
Status of loans in execution	<a href="http://ops/approvals/pdfs/PEen.pdf">http://ops/approvals/pdfs/PEen.pdf</a>
Tentative lending program	<a href="http://opsgs1/ABSPRJ/tentativelending.ASP?S=PE&amp;L=EN">http://opsgs1/ABSPRJ/tentativelending.ASP?S=PE&amp;L=EN</a>
Information available in the RE3/SC3 technical files	<a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=814338">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=814338</a>
Outcomes matrix	<a href="http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=837026">http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=837026</a>
Policy letter	<a href="http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=837030">http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=837030</a>

## ABBREVIATIONS

APW	Annual payment for works
APWM	Annual payment for works maintenance
COPEX	Comité de Programación de Concertaciones Externas del Sector Público [Programming Committee for Public-sector External Arrangements]
DASC	Dirección de Asuntos Sociales y Comunitarios [Social and Community Affairs Department]
DGPM	Dirección General de Programación Multianual del Sector Público [General Directorate of Multiyear Programming for the Public Sector]
DNCP	Dirección Nacional de Contabilidad Pública [National Public Accounting Office]
DNEP	Dirección Nacional del Endeudamiento Público [National Public-sector Borrowing Office]
DNPP	Dirección Nacional del Presupuesto Público [National Office of the Budget]
GDP	Gross domestic product
GPSE	Government Procurement System Evaluation
IAMS	Integrated Administrative Management System
IFMS-PS	Integrated Financial Management System for the Public Sector
IIRSA	Initiative for the Integration of South American Regional Infrastructure
IMF	International Monetary Fund
MEF	Ministry of Economy and Finance
MINSA	Ministry of Health
MMF	Multiyear macroeconomic framework
MPIP	Multiyear public investment program
MTPE	Ministry of Labor and Employment Promotion
PCM	Prime Minister's Bureau
PIP	Public investment project
PPP	Public-private partnership
PRODEV	Program to Implement the External Pillar of the Medium-term Action Plan for Development Effectiveness
PROINVERSION	Agencia de Promoción de la Inversión Privada [Private Investment Promotion Agency]
SENASA	Servicio Nacional de Sanidad Agraria [National Agricultural Health Service]
SNIP	National Public Investment System
SOSEM	Operating System for Monitoring and Evaluation
SSEGP	Public Expenditure Monitoring and Evaluation System
UCPS	Unidad de Coordinación de Préstamos Sectoriales [Sector Lending Coordination Unit]

## PROJECT SUMMARY

### PERU PROGRAM TO IMPROVE THE QUALITY OF PUBLIC MANAGEMENT AND EXPENDITURE II (PE-L1017)

Financial Terms and Conditions <sup>1</sup>				
Borrower: Republic of Peru Executing agency: Ministry of Economy and Finance (MEF)			Amortization period:	20 years
			Grace period:	5 years
			Disbursement period:	12 months
Source	Amount (in millions)	%	Interest rate:	LIBOR
IDB (Ordinary Capital)	US\$200	100	Inspection and supervision fee:*	0%
Total	US\$200	100	Credit fee:	0.25%
			Currency:	Single Currency Facility
Project at a glance				
<b>Project objective:</b> The objective of this second programmatic operation is to continue supporting the Government of Peru in carrying out institutional, operational, legal, and regulatory changes to improve the quality of public management and expenditure by strengthening government capacities to analyze and monitor aspects relating to regulation, budget, public investment, and administrative management and to promote greater private sector participation alongside the public sector in investment and in service delivery.				
<b>Special contractual conditions:</b> See Conditionality Matrix in Chapter V. (5.1)				
<b>Exceptions to Bank policies:</b> None.				
<b>Project consistent with country strategy:</b> Yes [ X ]                      No [ ]				
<b>Project qualifies as:</b> SEQ [ ]                      PTI [ ]                      Sector [ ]                      Geographic [ ]                      Headcount [ ]				
<b>Verified by CESI on:</b> 16 June 2006				

<sup>1</sup> The interest rate, credit fee, and inspection and supervision fee mentioned in this document are established pursuant to document FN-568-3 Rev. and may be changed by the Board of Executive Directors, taking into account the available background information, as well as the respective Finance Department recommendations. In no case will the credit fee exceed 0.75%, or the inspection and supervision fee exceed 1% of the loan amount.\*

\* With regard to the inspection and supervision fee, in no case will the charge exceed, in a given six-month period, the amount that would result from applying 1% to the loan amount divided by the number of six-month periods included in the original disbursement period.

## I. FRAME OF REFERENCE

- 1.1 This loan operation is the second of three consecutive single-tranche operations that, while technically related, are being financed independently under the programmatic policy-based lending approach in accordance with documents CA-450-1 and CS-3633. On 7 December 2005 the Board of Executive Directors of the Bank approved the first policy-based loan (PBL) in this programmatic series entitled “Program to Improve the Quality of Public Management and Expenditure” (loan 1699/OC-PE), for US\$200 million, which was disbursed in late December 2005. The proposal for that loan constitutes the **framework document** for the programmatic series (PR-2997), and the present proposal updates, complements, and follows up on the framework document, in accordance with the guidelines set forth in Memorandum EVP/1/2006 (PO-LO-2006) dated 6 March 2006.

### A. General context

- 1.2 Peru’s economic indicators are remarkably stable, thanks to responsible fiscal management and political consensus on the importance of maintaining a sustainable macroeconomic context. In 2005 gross domestic product (GDP) grew 6.4% and the economy completed four years of continuous growth with an average rate of 5.2%. The deficit of the nonfinancial public sector was 0.3% of GDP, the rate of inflation was 1.5%, and the exchange rate remained stable with considerable monetary reserves. Peru has also met the targets of its 2004 stand-by arrangement with the International Monetary Fund (IMF).
- 1.3 Peru’s international liquidity position is sound, thanks to a balance of net international reserves at the end of 2005 of US\$14.097 billion—an increase of US\$1.466 billion over the close of 2004. Net international reserves represent about 14 months’ worth of goods imports. Meanwhile, the trade surplus was US\$5.163 billion in 2005 and is expected to be over US\$6 billion in 2006. Moreover, the country risk has decreased in recent years from an average of 615 points in 2002 to 199 in 2005.
- 1.4 Public debt in June 2006 was US\$28.22 billion, including US\$22.039 billion in external liabilities and US\$6.181 billion in internal liabilities. As a percentage of GDP, total public debt fell from 45% in late 2004 to 38.2% at the end of 2005, mainly due to GDP growth in dollars and the depreciation of the yen and euro relative to the dollar. External public debt decreased by 7 percentage points of GDP to 28.1%, as a result of the aforementioned factors and prepayments by the government to the Paris Club (US\$1.555 billion) and the Japan Peru Oil Company (US\$757 million).
- 1.5 As for the external debt profile, 35.2% of commitments as of June 2006 were to multilateral entities, and the total average annual service on the debt for the next six years is US\$2.6 billion (equivalent to 2.7% of GDP), which means that US\$1.022 billion in external resources is needed for 2006, and US\$1.078 billion for

2007. The current debt level is considered sustainable over the medium and long terms, and is indicative of the country's progress in stabilizing public finances.<sup>1</sup>
- 1.6 In general, while short- and medium-term macrofinancial performance has been solid, further measures should be taken to help achieve sustained economic growth. Increased capital accumulation, labor productivity, and efficiency in the use of capital and the current account are encouraging signs that the country has a foundation for growth, which should continue to be developed.
  - 1.7 In 2005 public investment totaled 2.9% of GDP (2.8% in 2004), and private investment, 16% (15.3% in 2004). These figures are lower than the recent highs of 4.8% (public investment in 1994) and 19.2% (private investment in 1995). Peru has one of the lowest investment levels in the region, and more and better public and private investment is urgently needed.
  - 1.8 The activities begun in 2005 under the first operation in the programmatic series have been building the legal and institutional framework to allow the government to make public expenditure impact and efficiency gains, and to find a sustainable and responsible way of promoting private investment alongside the public sector. The program should help promote high, sustainable investment and growth rates that are consistent with an inclusive, equitable pattern of development.

## **B. Specific problems and Peru's strategies and actions for addressing them**

- 1.9 This section describes and examines the actions that the Government of Peru has been taking in the strategic areas set forth in the 2005 framework document. Program objectives and targets may be found at this link for the [Outcomes Matrix](#).

### **1. Private-sector participation in public investment**

- 1.10 During the first operation of this programmatic series in 2005, the Ministry of Economy and Finance performed an evaluation of the institutional, operational, legal, and regulatory framework for public-private partnerships (PPPs),<sup>2</sup> and published a proposed strategy and management structure for projects to be financed as PPPs.
- 1.11 As part of this evaluation, institutional, fiscal, and accounting measures have been taken. The main **institutional measures** have been aimed at improving mechanisms for coordinating, establishing processes, and strengthening capacities. The MEF—in order to clarify institutional duties and develop new procedures for PPP project approval and to strengthen its duties in performing ex ante evaluations of the viability of such projects—has designated the General Directorate of Multiyear Public-Sector Programming (DGPM) as the entity responsible for coordinating PPP projects.

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<sup>1</sup> Source of macroeconomic data: Multiyear Macroeconomic Framework 2007-2009 (<http://www.mef.gob.pe>).

<sup>2</sup> Under Peruvian law these are termed “cofinanced concessions”, in accordance with Executive Decree 059-96-PCM.

- 1.12 The strategic guidelines for strengthening sector capacities, as published in 2005, set forth the need to have expert advisers in structuring complex projects, strengthening the capacity and experience of PPP teams in designing advanced projects; business analysis methodologies; value-for-money assessment; complex financial engineering; and economic, technical, financial, and contractual issues to be incorporated into the project cycle.
- 1.13 As for **fiscal measures**, the General Law on the National Debt System (Law 28563 of 2005) established provisions on treatment and recording of liabilities and guarantees for PPPs, and the Law to Facilitate the Financing of Processes to Promote Private Investment and Concessions (Law 28742) provided that the annual flow of firm and contingent financial commitments from the national government that are derived from the promotion of private investment and concessions may not exceed 0.5% of GDP per year. Also, the Multiyear Macroeconomic Framework (MMF) was required to contain information on definite and contingent commitments of PPP projects.
- 1.14 As for **accounting measures**, the Government of Peru has been developing methodologies for accounting and controlling expenditures on PPPs, by quantifying risks and assessing contingent liabilities resulting from investment contracts with the private sector, along with the corresponding recording and monitoring of liabilities and guarantees generated in the PPP process. This has made it possible to move toward more sophisticated methods of risk allocation.
- 1.15 These measures have been very important, as they not only promote private investment alongside the public sector, but they do so in a framework of fiscal prudentialism and transparency, helping PPP projects to move ahead and at the same time not compromising the State's future payment capacity.
- 1.16 The new PPP projects that Peru has been carrying out, the progress of which has begun to be reflected through the Costa-Sierra program, enjoy greater MEF engagement from the initial phase of the project cycle in terms of determining economic and social viability and whether projects should be carried out as PPPs, and in terms of a greater identification, allocation, and mitigation of technical and fiscal risks over the short and medium terms; and the assessment and monitoring of actual and contingent liabilities.

## **2. Public expenditure management at the national level**

- 1.17 In December 2005 the Peruvian Congress passed the Public Sector Budget Act for Fiscal Year 2006 (Law 28652), which it Act authorized the development of the following instruments: cost-based budgeting and a competitive fund—through pilot programs—to allocate resources related to performance; and the results-based management contracts to be signed with operational units.
- 1.18 These interventions are aimed at upgrading and modernizing the budget management system to create incentives for optimal allocation and execution of resources. At the end of 2005, the National Office of the Budget (DNPP) of the



MEF prepared and approved specific strategies for each instrument, detailing the methodologies and procedures for the pilot programs and the overall implementation strategies.

- 1.19 Also, on 9 February 2006, the Bank and the government signed the letter of agreement for the **PRODEV** technical-cooperation operation, “Strategy and Action Plan for Development Effectiveness and Results-based Management in Peru” (ATN/OC-9534-PE), the objective of which is to help strengthen results-based management in the Peruvian government as a way of promoting efficiency in public-sector decision-making processes, and transparency and effectiveness in public expenditure, by supporting the preparation of a strategy and an action plan on this issue. Activities under that technical-cooperation operation are coordinated with the government’s results-based budgeting strategy, and complement and strengthen the development of instruments for evaluating public expenditure, the mechanisms for accessibility and quality of management and statistical information for the decision-making process, and a strategy to minimize regulatory obstacles and promote transparency and flexibility in public management.
- 1.20 Meanwhile, to strengthen the **prioritization and management of public investment**, the Public-Sector Budget Act for Fiscal Year 2006 authorized the DGPM to set guidelines for developing Multiyear Public Investment Programs (MPIPs), as well as any rules and guidelines needed to implement them.
- 1.21 As for the processes of approving **external loan operations to finance public investment projects (PIPs)**, a ministerial resolution established the Programming Committee for Public-sector External Arrangements (COPEX), which is chaired by the Deputy Minister of Finance and consists of the Deputy Minister of Economy and the General Directors of the National Public-sector Borrowing Office (DNEP), the DNPP, the General Directorate of Economic and Social Affairs (DGAES), and the DGPM. The DNEP serves as the technical secretariat of COPEX.
- 1.22 COPEX’s duties are to set guidelines for arranging external-debt operations to finance PIPs and to propose the Three-Year Program of External Arrangements and the Three-Year Disbursement Schedule, and verifying that they are consistent with the priorities of the MMF.
- 1.23 Through a November 2005 ministerial resolution, the **Operating System for Monitoring and Evaluation (SOSEM) of the National Public Investment System (SNIP)** was approved. It is mandatory for executing units in entities and firms in the nonfinancial public sector of the national government and regional governments. The purpose of SOSEM is to verify progress in project execution and consistency with the preinvestment studies supporting the ruling that these projects were viable.
- 1.24 SOSEM records information on costs, physical and financial targets in execution plans, contracts, and assessments. To this end, a specific computer application was developed that is compatible with the other SNIP tools. It has been developed based on pilot programs carried out in various sectors and regional governments.

- 1.25 As for the **plan to improve the quality of rules and regulations**, the criteria for beginning the pilot project in the MEF were released in late 2005. Activities in this area include the stages for setting the objective of the rule being analyzed, weighing options, cost-benefit analysis, prior publication, public consultation, and proposal review.
- 1.26 With respect to improving **crosscutting management systems**, actions related to modernizing the **Integrated Financial Management System for the Public Sector (IFMS-PS)** have been advanced. In late 2005 the Bank supported the MEF in conducting a preliminary diagnostic assessment of the IFMS-PS and developing terms of reference for an independent evaluation of the system to help coordinate a strategic plan for modernization.
- 1.27 Another important crosscutting management system included in this second operation of the programmatic series is that of **government procurement**, which was the subject of the Government Procurement System Evaluation (GPSE), prepared with support from the IDB and the World Bank and included a broad assessment and plan of action for the sector that were agreed to with Peru in late 2005.

### **3. Public expenditure management in the context of decentralization**

- 1.28 The Government of Peru has been evaluating and designing instruments conducive to budgetary and institutional reform to ensure fiscal neutrality in the decentralization effort, i.e., whereby transfers of resources to subnational levels, to go along with the corresponding duties and areas of responsibility, are equivalent to the reduction in budgetary resources at the national government level. In this regard, information on decentralization in Peru needs to be decentralized, with emphasis on the five-year plans for transferring duties and responsibilities and the corresponding budget horizon.
- 1.29 As for the stabilization of transfer flows to regional and local governments, in 2005 the Executive Branch submitted to Congress the bill on the Stabilization Fund for Shareouts, Royalties, and the Camisea Socioeconomic Development Fund (FOCAM).
- 1.30 Lastly, regarding the regional governments' capacity to evaluate preinvestment studies, it is estimated that in 2004-2005 only 35% of the projects ruled viable by their investment programming offices were effectively analyzed according to the methodologies established in the SNIP. Thus, the MEF has been supporting these governments in upgrading their ability to analyze and prioritize investment.

### **C. The Bank's sector and country strategies**

- 1.31 There were no changes in how this program relates to the Modernization of the State Strategy (OP-1004) and Competitiveness Strategy (OP-1005), or to the country strategy (document GN-2205-1), from the **framework document** (PR-2997) for the programmatic series approved in 2005.

#### **D. Program strategy**

- 1.32 **Programmatic approach.** In accordance with the **framework document** (PR-2997) approved by the Bank's Board of Executive Directors in December 2005, the programmatic approach is justified because the implementation of reforms to tackle the problems identified warrants a medium- and long-term execution period. The strategy for this second operation is to promote continuity in the reforms begun in 2005 during a change of administration, by strengthening and promoting the sustainability of the 2005 measures and making them operational.
- 1.33 **Coordination with other Bank operations.** This second operation under the programmatic approach complements the focus of the policy-based loans approved for Peru in recent years, as described in the **framework document** (PR-2997). This second operation is also supported by other Bank projects, such as: (i) Institutional Sector Facility to Improve the Quality of Public Management and Expenditure in Peru (loan 1696/OC-PE); (ii) PRODEV nonreimbursable technical-cooperation operation ATN/OC-9534-PE; and (iii) the State Modernization and Decentralization Program (loan 1437/OC-PE), among other projects. Also, through the technical-cooperation operation "Peru Elections 2006: Strengthening National Debate" (ATN/FT-9218-PE) several documents and technical proposals have been discussed with political parties and other stakeholders during the 2005-2006 election season, including several issues from this programmatic series.
- 1.34 The program also complements Bank operations to promote investment in infrastructure with private-sector support, such as the guarantee program for the IIRSA Northern Amazon Hub (loan 1717/OC-PE), approved in February 2006 and which supports a PPP project by providing a guarantee for the government's payment commitments to the concessionaire.
- 1.35 **Lessons learned.** Evaluations and studies on the effectiveness and impact of policy-based loans suggests that the effectiveness of programs of this kind depends to a large extent on the degree of government commitment to the proposed reforms. In this regard, the programmatic approach has been effective in promoting continuity in the reform processes and activities included in the program during the government transition period, as shown in the policy letter for 2006.

#### **E. Coordination with other donors**

- 1.36 In preparing this second operation, the team has maintained a high level of multilateral coordination with specialists from the IMF and the World Bank, both at Headquarters and in Peru, and it has also assured close coordination with the Andean Development Corporation and other stakeholders.
- 1.37 With respect to the IMF, a workshop on financial management systems was held in Washington, D.C. on 19 June 2006 in conjunction with the IDB and the World Bank, where specific issues related to this second operation were discussed. The Andean Development Corporation, in turn, has granted financing for activities

related to competitiveness, including the development of the corresponding policies, which in turn includes the strengthening of the institutional, operational, legal, and regulatory framework for PPPs.

- 1.38 The World Bank has provided financing to strengthen the fiscal decentralization process in terms of improving monitoring and evaluation of the public finances of regional and local governments, participatory budgeting, and strengthening of capacity to identify, develop, and perform ex ante evaluations of investment projects.

## II. THE PROGRAM

### A. Objectives and description

- 2.1 The objective of this second programmatic operation is to continue supporting the Government of Peru in carrying out institutional, operational, legal, and regulatory changes to improve the quality of public management and expenditure by strengthening government capacities to analyze and monitor aspects relating to regulation, budget, public investment, and administrative management and to promote greater private sector participation alongside the public sector in investment and in service delivery.
- 2.2 The general idea is to take advantage of the synergy between reforms that will improve budget and public-debt management and the new public-private partnership (PPP) policy, while at the same time enhancing the quality of current and capital expenditure, both exclusively public spending and public-private spending.
- 2.3 Successful implementation of the reforms included in this program presupposes a stable macroeconomic environment that is compatible with the program's objectives and consistent with the forecasts in the Multiyear Macroeconomic Framework 2007-2009 (<http://www.mef.gob.pe/>). The amounts proposed are in line with government and IMF forecasts in terms of external financing needs for this year and the coming years, and with the financial requirements for 2006 set forth in Bank programming.<sup>3</sup>
- 2.4 As stated in paragraph 1.5, Peru needs US\$1.022 billion in external resources for 2006, and US\$1.078 billion for 2007. This need would be covered by the possible bond issue and with support from multilateral organizations. The Sources and Uses Matrix is available in Table 6 of the MMF 2007-2009 (<http://www.mef.gob.pe/>).

### B. Components

- 2.5 This section describes each program component, as well as adjustments to the triggers established in the 2005 framework document. In general the changes were minimal, due to the Bank's successful dialogue process with the new Peruvian government, and do not affect the program's medium- and long-term objectives. This section also describes the progress made in each specific component and subcomponent as of the analysis mission in September 2006, showing 90% completion of the technical and political effort needed to meet the conditions for 2006. The Government of Peru has stated to the Bank, however, its intention of fulfilling all conditions by the end of 2006.

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<sup>3</sup> The US\$450 million called for by the Bank's programming for 2006 would be provided by US\$200 million for this operation, US\$100 million from the last tranche of the 2003 Competitiveness Reform Program (loan 1503/OC-PE), and US\$150 million from the last tranche of the 2004 Poverty Alleviation and Human Capital Development Program (loan 1600/OC-PE).

## 1. Macroeconomic stability

- 2.6 The objective of this component is to continue to ensure a macroeconomic environment that is consistent with program objectives. Fulfillment of this condition will be confirmed through information supplied by the MEF on progress in implementing its economic policy, which includes among other things the results of the latest performance review under the stand-by arrangement with the IMF.<sup>4</sup> Also, in October 2006 the Bank approved its [macroeconomic assessment](#) for Peru.

## 2. Private-sector participation in public investment

- 2.7 The **general objective** of this component is to achieve a sustainable increase in the quantity and quality of investment in the country's infrastructure, through greater participation by the private sector in public investment, and to make investment more efficient. To this end, the program will support policies to establish a conceptual model for PPPs that will promote fiscally prudent efficiency in public expenditure.
- 2.8 The **specific objective** of this component in this **second operation** is to strengthen the aspects related to the new institutional framework to support the structuring of more efficient PPP processes, with effective systems for identifying and mitigating risks, including modern mechanisms for monitoring and controlling contingent liabilities and competitive bidding procedures.
- 2.9 The first operation established as a **trigger** for 2006 an **institutional, operational, legal, and regulatory PPP framework** implemented according to targets and criteria agreed upon with the Bank, including the following aspects: (i) intra- and interagency coordination mechanisms established and in operation; (ii) methodologies for selecting projects to be financed as PPPs implemented (considering SNIP criteria); (iii) review of procedures for selecting firms to execute PPPs, considering the establishment of minimum timetables for specific stages and GPSE recommendations; and (iv) a system for recording liabilities and guarantees generated in the process of promoting private investment and concessions, including PPPs, implemented and in operation.
- 2.10 As for the (i) **coordination mechanisms**, the MEF has taken measures to strengthen intra- and interagency coordination by implementing procedures to coordinate PPP-related activities among the various agencies inside the MEF itself and with other institutions such as PROINVERSION, sectoral ministries, and regulatory bodies. The MEF recently published new guidelines for the provision of public services through PPPs ([http://www.mef.gob.pe/INFECO/documentos/Concesiones\\_Cofinanciadas.pdf](http://www.mef.gob.pe/INFECO/documentos/Concesiones_Cofinanciadas.pdf)), with a breakdown of competencies and procedures for the entire PPP cycle, which is to become a ministerial resolution.

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<sup>4</sup> At its meeting on 8 February 2006, the Executive Board of the IMF completed its third review of the stand-by arrangement for Peru (<http://www.imf.org/external/pubs/cat/longres.cfm?sk=18875.0>) and in July 2006 the final review was completed (<http://www.imf.org/external/np/sec/pr/2006/pr06170.htm>).

- 2.11 As for the (ii) **PPP methodologies**, the MEF has been developing knowledge for the selection of PPP projects, including criteria for measuring and monitoring the value for money offered by such projects (delays in this process have been offset by developing a methodology for assessing contingent risks, maintaining the policy reform effort put forth for this issue). As for (iii) **selection procedures**, PROINVERSION has approved a policy regulating the processes for selection and hiring of firms for executing PPPs, including timetables for issuing documents to bidders prior to receiving the proposals and for issuing reports from the Office of the Comptroller General and from regulatory bodies.
- 2.12 Lastly, the (iv) system for **recording liabilities and guarantees** was developed and implemented at the DNEP and has begun operating, thereby allowing for centralized monitoring of fulfillment of the established ceiling of 0.5% of GDP with annual payments from the firm and contingent financial commitments from the national government resulting from the promotion of private investment and concessions.

### **3. Public expenditure management at the national level**

- 2.13 The **general objective** of this component is to help strengthen the national government's capacity to manage, analyze, prioritize, execute, monitor, and evaluate public spending, primarily capital spending. The program has been supporting reforms to enhance quality in management of the budget, public investment, regulation, and crosscutting administrative management systems.
- 2.14 The **specific objective** of this component **in this second operation** is to begin implementing **results-based budgeting**, to continue progress in improving prioritization and **public investment management**, to increase coverage of mechanisms for monitoring **regulatory quality**, and to modernize the **crosscutting financial management** and procurement **systems**.
- 2.15 **Results-based budgeting.** To modernize the budget management system and generate performance incentives for optimal allocation and execution of resources, the program framework document, approved in 2005, established as a **trigger** for 2006 a **results-based budget** at the beginning of implementation, including the following aspects: (i) pilot cost-based budgeting project in executing units and the competitive fund for allocating budgetary resources, in operation, and six results-based management contracts signed and being executed; (ii) the Public Expenditure Monitoring and Evaluation System (SSEGP) implemented at the national government level; (iii) action plan for results-based management approved; and (iv) pilot project for evaluating institutional management implemented and evaluated.
- 2.16 Progress in each of these aspects is: (i-1) *cost-based budgeting*—the MEF has concluded the cost-based budgeting pilot program with the National Agricultural Health Service (SENASA), and after the pilot project is evaluated, these elements should be gradually incorporated into budgeting regulations for the following year; (i-2) *competitive resources*—while the pilot program for the competitive fund was

not carried out, the Directive on Programming and Developing the Budget for National Government Bidding Documents for Fiscal Year 2007 includes provisions for adopting technical criteria and mechanisms for all allocations of incremental budget resources associated with new activities and projects, which maintained the policy reform effort set forth for this issue; (i-3) *results-based management contracts*—the MEF has signed and posted on its website results-based management contracts with 26 educational institutions, 18 hospitals, and 11 police stations, including the payment of productivity bonuses for good performance; (ii) *SSEGP*—networked computer application implemented in the national government and formalized through the aforementioned Directive (2007) and the Evaluation Directive (2006) of the Institutional Budgets of the National Government and Regional Governments that requires the use of indicators to measure and evaluate institutional performance, which supports the determination of outputs and outcomes to be achieved with the budget allocation; (iii) *Action plan for results-based management*—pursuant to a ministerial resolution of the Prime Minister’s Bureau, the Advisory Committee for Strengthening Results-based Management was created in March 2006, and with support from the Bank and resources from PRODEV, it has developed and approved “Guidelines for Results-based Public Management,” which includes the basic tenets of an action plan for results-based management; and (iv) pilot program for evaluating institutional management—this action was pushed back to 2007 due to operational and financing problems (which have been resolved for 2007), which does not affect the proposed general objective of results-based budgeting that has begun to be implemented.

- 2.17 **Public investment management.** To strengthen the process of analyzing, prioritizing, executing, monitoring, and evaluating public investment in order to improve efficiency and quality, the following **triggers** were established for 2006: (i) the Evaluation Committee reviews and makes adjustments to the criteria for selecting debt operations associated with PIPs and PPPs; (ii) overall ceilings and sector amounts for public investment loan disbursements for 2007-2009 incorporated into the MMF, including those for contingent liabilities and certain ones associated with PPP operations; and (iii) improvements in PIP preparation, monitoring, and evaluation, including those aspects detailed in paragraph 2.20.
- 2.18 COPEX (initially called the Commission for Evaluating Public Investment Projects) has been established and is operating, and approved its operating regulations, the annual program for arranging external and internal loans for 2006 (posted on the MEF website), and the guidelines for the three-year arrangement of external loan operations for financing PIPs.
- 2.19 The MMF 2007-2009 includes *overall* public investment *ceilings*, as well as commitments associated with PPP operations (annual payments for works and annual payments for works maintenance). Also, in order to strengthen the investment selection process, the following have been established: a procedure for annual reviews of multiyear public investment programs (MPIPs), criteria for



- prioritizing the inclusion of projects in the MPIP, and consideration of the cost of maintaining capital goods.
- 2.20 For *improving PIPs*, the program's framework document includes the following aspects: (i) SOSEM implemented in three sectors; (ii) mechanisms in place to ensure that the PIPs' objectives are fulfilled and provide budgetary protection for efficient executing units; (iii) methodology for ex post evaluation applied to a sample of PIPs; (iv) mechanisms established for financing preinvestment of PIPs, such as a preinvestment fund; and (v) specific methodologies developed and disseminated for formulating and evaluating PIPs in the three sectors identified.
- 2.21 Progress in each of these aspects is as follows: (i) *SOSEM*—implemented not only in three sectors but throughout the nonfinancial public sector of the national government and regional governments with the processes and the computer application for the system validated through the pilot program and formalized through an agency resolution (the government entities are accessing the system through the website by using a code provided by the DGPM); (ii) *efficient executing units*—the MEF has issued an official letter to improve management of the executing units, which makes it mandatory to create boards of directors for the PIPs with external loans, and implementing rules for the competitive selection of coordinators and for approving and monitoring annual work plans; (iii) *ex post evaluation*—the MEF has already begun developing the methodology; however, given the timetable for this consulting contract, the commitment was moved to 2007; (iv) *preinvestment financing*—in the regional and local governments the Budget Act for Fiscal Year 2006 authorized use of a percentage of the resources from mining shareouts and royalties to finance preinvestment studies, which is maintained in the bill for 2007; and in the national government, the DGPM has been developing a proposal for other mechanisms to finance preinvestment; and (v) *PIP methodologies*—the DGPM has completed the three methodologies for developing and evaluating PIPs and expects to commission the preparation of others.
- 2.22 **Regulatory quality.** Activities in this area are intended to enhance the transparency, efficiency and quality of regulations in general, through adoption of an institutional and operational system of filtering procedures for quality control, including developing methodologies for economic impact analysis. During the first phase of implementation of these activities in 2005, the Government of Peru designed and approved an approach for ensuring quality in MEF regulations. The implementation of the institutional and operational approach for filtering procedures for quality control of policies in at least two additional sectors was set as a **trigger** for 2006; and the pilot MEF system was evaluated, and measures for improving it have been adopted.
- 2.23 The Government of Peru has implemented the aforementioned institutional approach to the policies issued by the MEF, and has carried out pilot programs in the Ministry of Health and the Ministry of Labor and Employment Promotion, which will serve as the basis for developing a methodology to be applied

throughout the Executive Branch. The new methodological guide for the MEF has been developed and will be approved by administrative resolution to ensure that its regulations, before being passed, are subjected to a series of controls for legal, economic, and administrative quality assurance.

- 2.24 **Crosscutting management systems.** In order to streamline and simplify procedures relating to crosscutting management systems in line with the rules issued by their governing bodies, a gradual strategy was developed that begins with modernization of the IFMS-PS, followed by the inclusion of other systems. In this regard, the following **triggers** were established for 2006: (i) recommendations for the logistics and asset control systems, implemented according to agreed targets, and the Integrated Administrative Management System (IAMS) implemented in 16 additional executing units; (ii) improvements in the management systems implemented, and assessment of and recommendations on another additional crosscutting system; and (iii) modernization of the IFMS-PS begun (as described in paragraph 2.27).
- 2.25 As for implementation of the IAMS in 16 additional executing units, the MEF has surpassed this target in 2006. However, the IAMS is part of a larger IFMS-PS strategy and in this regard should be assessed with the proposed process to modernize the IFMS itself.
- 2.26 Another crosscutting management system included in this second operation of the programmatic series is that of procurement, which includes passing regulations and corporate procurement, under the idea of centralizing some processes for bidding out specific products or services, maintaining decentralized procurement. The Prime Minister's Bureau has carried out pilot processes for corporate procurement that generated savings of 15%.
- 2.27 For *modernization of the IFMS*, the following **triggers** were set for 2006: (i) full integration of budgeting modules in the IFMS-PS; (ii) accounting process in the IFMS-PS fully automated by implementing a new budgetary classification based on international standards, and harmonization with a new chart of accounts; (iii) an action plan for modernizing the IFMS-PS approved, based on an independent evaluation that will take into account the incorporation of modules, changes in technological architecture, and a technical, functional, and economic feasibility analysis of the various alternatives; and (iv) model of a consolidated cash account designed and an action plan for implementing it.
- 2.28 Progress in each of these areas is as follows: (i) *integration of the budget*—the budgetary modules for development, amendments, and quarterly allocation have been integrated into the IFMS-PS; (ii) *accounting automation*—the new budgetary classification needed to further automate accounting records should be completed in 2006, and the IMF has supported the development of an action plan that provides a breakdown for implementation (part of this measure was pushed back to 2007); (iii) *IFMS Action Plan*—the MEF will hire a firm to perform the independent evaluation and prepare the IFMS Modernization Plan (financed by loan

1437/OC-PE). Once this evaluation is complete the MEF should review the recommendations (and their alternatives) for implementation, with the target of having an upgraded version of the system for fiscal year 2008 (action plan partially moved to 2007); and (iv) *consolidated account*—the IMF supported the Government of Peru in conceptualizing the consolidated cash account to make cash management more efficient, and the MEF has submitted an action plan for implementing it.

- 2.29 These interventions for improving public financial management are supported by two laws that were recently passed (in February 2006): the National Treasury System Act and the National Government Accounting System Act. These two laws complete the legal framework for public financial management set forth in the Public Sector Financial Management Framework Law (Law 28112) of 2004, which the Bank supported through operation 1412/OC-PE.

#### **4. Public expenditure management in the context of decentralization**

- 2.30 The **general objective** of this component is to stabilize revenue transfers by the national government to the regional and local governments and to improve the quality of expenditure management in general at this level of government. Also, progress in decentralization should be evaluated from an economic perspective, based on indicators of economic activity.
- 2.31 The **specific objective** of this component **in this second operation** is to make progress in **subnational fiscal stabilization**, promote **sustainability of the indices** of regional economic activity; establish **criteria for incentives-based budgetary reform**; and improve **regional governments' analysis and investment capacity**.
- 2.32 The first operation in the programmatic series in 2005 established the following **triggers** for 2006: (i) implementation of the Subnational Fiscal Stabilization Fund, including development of a study to analyze options that optimize, if necessary, the calculation of the benchmark value for transfers; (ii) estimation of the index of regional economic activity for all regions for the period 1970-2005; (iii) development of dissemination measures to implement specific instruments (for incentives-based budgetary reform) as part of the diagnostic assessment, and adoption of an action plan for the gradual implementation of these instruments and beginning of implementation according to targets agreed upon with the Bank; and (iv) implementation of incentives to improve the capacity of regional governments' technical teams responsible for analyzing the investments.
- 2.33 **Subnational Fiscal Stabilization Fund.** The bill sent to Congress in 2005 to create the Fiscal Stabilization Fund was not passed during the latest legislative session; however, the MEF will attempt to resume coordination with Congress on this issue in 2007. Nevertheless, the expected impacts from implementing this fund for stabilizing the flow of execution of resources from shareouts, royalties, and the Camisea Socioeconomic Development Fund (FOCAR) are being obtained through

strict observance of the legal provisions of the budgeting and investment systems,<sup>5</sup> i.e., the counter-cyclical prevention impact expected with the creation of the fund is being achieved through other mechanisms for controlling expenditure at the regional and local levels, and the project team believes that these results will be maintained over the medium term.

- 2.34 **Departmental economic activity indices.** The MEF has finished estimating the economic activity index for every department in the country for the period 1970-2005 and plans to draft a proposal to ensure that, in the future, those rates are calculated regularly.
- 2.35 **Incentives-based budgetary reform.** The MEF, with support from the Bank, has been conducting a study to identify the budgetary impact of the decentralization process in national government agencies and to make progress in designing instruments for future adjustments in these agencies to help ensure the decentralization process has a neutral fiscal impact.
- 2.36 **Investment analysis capacities in regional governments.** The MEF, acting through the DGPM, has been supporting the regional and local governments to improve their capacities to develop and evaluate public investment projects, including plans for training, dissemination, technical assistance, preinvestment resources, regulatory framework, and specialized guidelines and methodologies.
- 2.37 **The triggers have been adjusted as follows:** of the 30 specific measures in the 2005 triggers, 23 have been fully met, many of them with significantly increased coverage and outcome targets; two actions were adapted, maintaining the policy reform effort (methodologies for the selection of PPPs and the budget for the competitive fund); and five actions were partially moved to 2007, one achieving the proposed impact through other actions (Subnational Stabilization Fund) and others with much of the effort needed for fulfillment already made (pilot project for institutional management in the design process, ex post evaluation methodology under development, accounting automation in the IFMS at an advanced stage, and the IFMS-PS Modernization Plan at the final procurement stage). These adjustments are reflected in the disbursement conditions for 2006 and do not affect the program's medium- and long-term objectives or the expected impact outcomes.

### **C. Cost and financing**

- 2.38 This loan operation is the second project under the programmatic policy-based lending approach and will be disbursed in a single tranche of US\$200 million.

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<sup>5</sup> Quarterly transfers in 2004-2005 have practically doubled in amount, and related expenditures on investment have increased approximately 35%.

### **III. IMPLEMENTATION**

#### **A. Borrower and executing agency**

- 3.1 The borrower is the Republic of Peru, and the executing agency is the Ministry of Economy and Finance (MEF). The National Public-sector Borrowing Office (DNEP) is responsible for negotiating the financial aspects of the operation, and the Sector Lending Coordination Unit (UCPS) will coordinate technical aspects of the program. The technical responsibilities shared by the various units of the MEF are the same as those set forth in the 2005 **framework document** (PR-2997), except in the case of PPPs, which are now the responsibility of the General Directorate of Multiyear Programming (DGPM).

#### **B. Execution and management**

- 3.2 Virtually all technical actions and decisions needed to implement the program are under the jurisdiction of the MEF, which through each of the corresponding bodies will be responsible for implementing decisions and specific measures.
- 3.3 The DNEP continues to be responsible for the financial aspects, including processing the disbursement, and the UCPS continues to be the technical body of the MEF in charge of, *inter alia*, coordinating among the various agencies of the MEF that are responsible for the technical execution of activities.

#### **C. Plan for executing the programmatic series**

- 3.4 Based on the fact that the program has been properly executed thus far and on the stated intention of the Government of Peru, the third operation may be approved in late 2007.

#### **D. Monitoring and evaluation**

- 3.5 There were no changes in the monitoring and evaluation mechanisms approved in the 2005 framework document for the programmatic series, and pursuant to Memorandum EVP/1/2006 (PO-LO-2006) sent to the Loan Committee on 6 March 2006, project performance monitoring reports will be prepared annually, one for each operation; and a single project completion report will be prepared at the end of the programmatic series.

#### **E. Policy letter**

- 3.6 The Bank and the Government of Peru have agreed on the sector and macroeconomic policies in the policy letter sent by the MEF in 2005. Also, the new administration in Peru has confirmed its commitment to program reforms and activities by updating the [policy letter](#) for 2006.

#### **IV. VIABILITY AND RISKS**

##### **A. Institutional and socioeconomic viability**

- 4.1 There have been no changes in the institutional and socioeconomic viability described in the 2005 **framework document** for the programmatic series.

##### **B. Environmental and social impact**

- 4.2 While the program has no negative social or environmental impacts, as part of the strategy for implementing the PPPs, the existence and capacity of the units responsible for preparing and subsequently supervising the environmental mitigation plans for addressing the direct and indirect impacts within the investment projects to be carried out has been verified. In this regard, PROINVERSION has a Social and Community Affairs Department (DASC), whose main duty is to lead consultation and information processes in project development. The DASC maintains direct contact with the regional and municipal governments, as well as with civil society. Also, through the Guarantee Facility, which was approved by the World Bank in April 2005, PROINVERSION has a methodology for performing social and environmental assessments of projects, which helps identify risk levels. The Ministry of Transportation and Communications also has an Environmental Affairs Department, and it is being strengthened through two sector operations: the Highway Rehabilitation and Improvement Program (PE-0197) and the Departmental Roads Program (PE-0236).

##### **C. Benefits and beneficiaries**

- 4.3 There have been no changes in the benefits and beneficiaries described in the 2005 **framework document** for the programmatic series.

##### **D. Risks**

- 4.4 Three main risks were identified in 2005: (a) the possible collapse of political support, which would mean that reforms might be slowed down, postponed or revised; (b) potential problems in implementing complex institutional changes; and (c) insufficient interagency coordination in planning and evaluation, considering the proposed process for institutionalizing a new National Strategic Planning System, which is under the Prime Minister's Bureau (PCM). Thus far none of these risks has materialized, and hence they are not expected to be an obstacle to the planned reforms. However, a new risk has been identified in relation to Law 27293 of 19 July 2006, which stripped the MEF of authority to declare PIPs technically viable. To mitigate any negative impacts, the MEF has been working on a bill to amend this law and other alternative regulations to maintain the quality of the SNIP.

## V. POLICY AND CONDITIONALITY MATRIX

- 5.1 The **policy matrix** approved in the 2005 **framework document** established the reform objectives for the period 2005-2007 and is still in effect. The conditions for 2006 for this loan were established based on the review of triggers established in 2005 and strengthened in the Conditionality Matrix for 2006 below. The rationale for the adjustments to this review process is presented in Chapter II under each specific component and subcomponent. Also, the triggers for 2007 were spelled out in greater detail (see Annex I).

Disbursement conditions for 2006	Means of verification
1. The overall <b>macroeconomic policy</b> framework is consistent with the program objectives and the guidelines established in the sector policy letter.	1. Information provided by the MEF and evaluated by the Bank.
2. <b>Institutional, operational, legal, and regulatory framework</b> for PPPs implemented in line with IDB-agreed targets and criteria, including: (i) inter- and intra-institutional coordination mechanisms up and running; (ii) methodological criteria for assessing contingent liabilities on projects to be financed as PPPs set; and (iii) procedures for selecting firms to execute PPPs reviewed.	2. (i) Regulations for Organization and Duties of PROINVERSION published in the Official Gazette El Peruano, specifying duties regarding the policy for promoting private investment; and the MEF's ministerial resolution approving the "Guidelines for provision of public services in cofinanced concessions," published in the Official Gazette El Peruano; (ii) approval of a report on assessment of contingent liabilities; and (iii) policy approved by PROINVERSION to regulate selection and procurement processes, including timetables for issuing documents to bidders prior to receiving proposals, and to issue reports from the Office of the General Comptroller and regulatory bodies.
3. System in place for <b>recording liabilities</b> and guarantees generated in the course of promoting private investment and concessions, including PPPs.	3. The Bank verifies that the system is in operation, that information on quantifiable commitments is recorded and that the DNEP has issued a communication instructing its departments to use the recording module.
4. <b>Results-based budgeting</b> is being implemented, including the following aspects: (i) a pilot in place for cost-based budgeting; criteria established for allocating incremental budgetary resources; and results-based management contracts signed; (ii) SSEGP implemented within the national government; and (iii) preliminary action plan approved for results-based management.	4. (i) Document on the pilot cost-based budgeting program approved by the DNPP; DNPP-MEF Directive for budget planning and formulation including criteria for allocating incremental resources, published in the Official Gazette El Peruano; and 55 results-based management contracts signed between the DNPP and expenditure executing agencies, and posted on the MEF website; (ii) MEF Directive for budget evaluation, that calls for the evaluation of SSEGP management and performance indicators published in the Official Gazette El Peruano; and (iii) the "Guidelines for Results-Based Public Management" are approved by the Advisory Committee for Strengthening Results-Based Management.
5. Guidelines and criteria for arranging external loan operations associated with PIPs and PPPs, established by <b>COPEX</b> .	5. COPEX minutes approving its operating regulations, and guidelines for arranging external loan operations to finance PIPs, posted on the MEF website.

Disbursement conditions for 2006	Means of verification
6. <b>Ceilings</b> on disbursement of loan proceeds for public investment for the 2007-2009 period incorporated into the MMF, including those for the APW and APWM associated with PPP operations.	6. The MMF 2007-2009 is published and includes ceilings; and an MEF Directive for programming and formulation of the budget for the national government's bidding documents for fiscal year 2007 includes instructions for strengthening multiyear public investment programming.
7. <b>Improved preparation, monitoring, and evaluation of PIPs</b> , including: (i) SOSEM implemented in projects under entities and companies in the nonfinancial public sector of the national government and regional governments; (ii) mechanisms in operation for ensuring that public investment projects meet their objectives and that efficient executing units enjoy budget protection; (iii) mechanisms in place for financing preinvestment in PIPs; and (iv) specific methodologies for formulating and evaluating PIPs developed and disseminated.	7. (i) Instructions for SOSEM published in the Official Gazette El Peruano and Bank verification of the use of the computer system by each sector; (ii) MEF Directive for budget planning and formulation for national government bidding documents for fiscal year 2007 has been published in the Official Gazette El Peruano and an official letter from the DGPM has been sent to the programming and investment offices to establish mechanisms related to the organization and management of executing units, aimed at ensuring fulfillment of objectives of public investment projects; (iii) Public Sector Budget Act for Fiscal Year 2006 includes provisions for financing preinvestment studies, and the proposal for 2007 maintains these provisions; and the preliminary proposal for other preinvestment financing mechanisms is approved by the DGPM; and (iv) three guides for formulating and evaluating PIPs are posted on the MEF website.
8. Implementation of the institutional and operational filtering procedures for <b>regulatory quality control</b> in two more sectors than in 2005. Pilot program for the system in the MEF is evaluated and filtering procedure for quality control for MEF standards, approved.	8. MEF guide for implementing regulatory quality control is posted on its website; reports on the previous regulatory pilot program in MINSA and the MTPE.
9. (a) <b>IAMS</b> is implemented in 16 more executing units than in 2005 and recommendations for the logistics and asset control systems are implemented. (b) Improvements in the crosscutting management system for <b>government procurement</b> are being implemented. (c) Modernization of the <b>IFMS-PS</b> has begun, including: (i) full integration of budgeting modules in the IFMS-PS; (ii) improvements in timely accounting; (iii) a firm has been hired to perform the independent evaluation of the IFMS-PS or call for proposals for hiring a firm, completed; and (iv) a model for a consolidated account has been designed and an action plan has been developed to implement it.	9. (a) MEF document and Bank verification of the IAMS system. (b) PCM document on implementation of the corporate procurement system, indicating the benefits of the system; and Executive Decree amending the regulations of the Procurement Act, making corporate purchasing mandatory, and the Corporate Purchasing Unit, published in the Official Gazette El Peruano. (c) (i) Bank verification of the system, checking that budget module has been integrated into the IFMS-PS; (ii) action plan for automated accounting, including the concept of timely accounting, in parallel with the budget execution process, is approved; (iii) contract signed with the consulting firm; or minutes from the Evaluation Committee on completion of the bidding process; and (iv) document on design of the consolidated account is approved by the DNTP.



Disbursement conditions for 2006	Means of verification
<p>10. (i) Less volatility in the <b>flow of expenditures</b> executed using shareout, royalties, and the Camisea Socioeconomic Development Fund (FOCAM).</p> <p>(ii) <b>Indices</b> of economic activity for all departments for the period 2001-2005 have been estimated by the MEF.</p> <p>(iii) Action plan for gradual implementation of instruments for <b>incentives-based budget reform</b> has been approved by the DNPP.</p> <p>(iv) Incentives for improving the capacities of technical teams charged with developing and evaluating public investment projects in <b>regional and local governments</b> is being implemented.</p>	<p>10. (i) MEF document on transfers to regional and local governments with the analysis of actual flow of transfers, including the evaluation of causes and the design of actions, mechanisms, and incentives for maintaining preventive counter-cyclical stability in future flows.</p> <p>(ii) Estimate of departmental economic activity from 2001 to 2004 is included in MMF 2007-2009; and DGAES report with indices calculated for 2005.</p> <p>(iii) DNPP document approved.</p> <p>(iv) DGPM document describing training, dissemination, technical assistance, regulatory framework, methodologies, and specialized guides for the use of regional and local governments.</p>

## **ANNEX I – TRIGGERS FOR 2007**

**A. Private-sector participation in public investment:** (i) new institutional, operating, legal, and regulatory framework for PPPs including implementation of specific methodologies to measure value for money and assessment of contingent liabilities is being applied to new PPP projects; and (ii) the module for recording PPP liabilities and guarantees includes information on actual and contingent liabilities of all active PPP projects under the national government and its use is extended to the sectors.

### **B. Public expenditure management at the national level**

**I. Results-based budgeting, monitoring and evaluation of public expenditure:** (i) development and application of a budgetary planning methodology in five national government bidding documents that incorporates results-based budgeting concepts and instruments and lessons learned in the cost-based budgeting pilot programs in 2006; (ii) design of a competitive fund for PIPs in regional and local governments; (iii) results-based management contracts have been evaluated, and the number of such contracts signed and being executed is increased; (iv) information entered in the SSEGP by all sectors allows for consolidated monitoring and evaluation reports to be generated that provide feedback for the budget preparation process; (v) action plan for results-based management is being implemented on schedule; and (vi) pilot program for evaluating institutional management has been implemented.

**II. National Public Investment System (SNIP):** (i) The MMF includes ceilings for disbursement of loan proceeds for public investment for the period 2008–2010, as well as contingent and actual liabilities associated with PPP operations; (ii) SOSEM incorporates information on project execution in sectors and regional governments; (iii) methodology for ex post evaluation is approved; and (iv) preinvestment financing mechanisms have been fully established.

**III. Improved regulatory quality:** Implementation of the institutional and operational system for regulatory quality control in two additional entities; and evaluation of the implementation of this system in the pilot programs at the MEF, MINSA, and MTPE.

**IV. Administrative management:** (i) inclusion of a new crosscutting management system for modernization, considering the possibility that it may be the Civil Service Payroll System; (ii) action plan for modernizing the IFMS is developed based on an independent evaluation, and implemented according to the timetable agreed upon with the Bank; (iii) chart of accounts brought into line with budget classification; and (iv) action plan for the consolidated account is being implemented.

### **C. Public expenditure management in the context of decentralization**

**I. Fiscal stabilization and regional economic growth:** (i) MEF document corresponding to condition 10(i) of 2006, regarding analysis of stability in transfers, has been updated; and the fund to improve regional compensation has been established; and (ii) the index of regional economic activity has been calculated for all departments for 2006.

**II. Incentives-based budgetary reform:** The 2008 budget calls for implementation of an action plan for budget reform in national government entities that will be decentralized this year, and contains preliminary multiyear forecasts consistent with the action plan. The action plan will promote a fiscally neutral impact on the transfer of services from the national government to the regional or municipal governments.

**III. Public investment at the regional level:** Evidence of an improvement in the quality of investment projects declared feasible by the regional governments.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-\_\_\_/06

Peru. Loan \_\_\_\_/OC-PE to the Republic of Peru  
Program to Improve the Quality of Public  
Management and Expenditure II

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Republic of Peru, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a program to improve the quality of public management and expenditure II. Such financing will be for an amount of up to US\$200,000,000 from the Single Currency Facility of the Ordinary Capital resources of the Bank, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

LEGIII/PE-814875-06  
PE-L1017