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PANAMA

PROGRAM TO STRENGTHEN FISCAL MANAGEMENT (PN-L1066)

LOAN PROPOSAL

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CONTENTS

PROJECT SUMMARY

I.	DESCRIPTION AND RESULTS MONITORING	1
A.	Background, problem addressed, rationale	1
1.	Macroeconomic performance	1
2.	Fiscal trends	2
3.	Fiscal management challenges	2
4.	Rationale	6
B.	The Bank's country and sector strategy	6
C.	Objectives	8
D.	Components and costs	8
E.	Key results indicators	10
II.	FINANCING STRUCTURE AND MAIN RISKS	10
A.	Financing instrument	10
B.	Coordination with other financing and donor agencies	11
C.	Environmental and social safeguard risks	11
D.	Other key issues and risks	11
III.	IMPLEMENTATION AND MANAGEMENT PLAN	12
A.	Summary of implementation arrangements	12
B.	Program execution and administration	12
C.	Summary of arrangements for monitoring results	14

ANNEXES	
PRINTED ANNEXES	
Annex I	Development Effectiveness Matrix (DEM) – Summary
Annex II	Results Matrix
Annex III	Fiduciary Agreements and Requirements
ELECTRONIC LINKS	
REQUIRED	
1.	Annual work plan (AWP) IDBDocs35765644
2.	Monitoring and evaluation arrangements IDBDocs35765682
3.	Procurement plan IDBDocs35770398
OPTIONAL	
1.	Implementation mechanism for program PN-L1066 IDBDocs35773063
2.	Sector note on results-based fiscal management (June 2010) IDBDocs35410639
3.	Brief notes on Panama’s fiscal reform IDBDocs35413419
4.	Report/diagnostic assessment of the General Revenue Directorate of Panama, CAPTAC/CIAT/IDB (June 2010) IDBDocs35773074
5.	Summary of the diagnostic assessment of the MEF General Revenue Directorate (February 2010) IDBDocs35773498
6.	Summary of the diagnostic assessment of the MEF Investment Programming Directorate (February 2010) IDBDocs35773115
7.	Cost-effectiveness analysis IDBDocs36213001
8.	IMF. 2010 Article IV Consultation – Staff report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Panama (October 2010) IDBDocs35413398
9.	IMF. Selected Issues Paper (October 2010) IDBDocs35413410
10.	MEF. Government Strategic Plan 2010-2014 IDBDocs35413373
11.	MEF. Fiscal reforms 2010 IDBDocs35413376

12. MEF. Law 8-2010, Tax reform
[IDBDocs35773473](#)
13. Law 34-2008, Fiscal and social responsibility
[IDBDocs35773487](#)
14. Program to strengthen fiscal policy and tax equity, 2473/OC-PN
[IDBDocs35457061](#)
15. Technical cooperation operation – Support to results-based management (ATN/OC-11401-PN)
[IDBDocs35773452](#)
16. Project completion report – Program to strengthen and modernize economic and fiscal management, phase II (1430/OC-PN)
[IDBDocs35773463](#)
17. World Bank. Technical assistance project for the improvement of public sector efficiency
[IDBDocs35823983](#)
18. Safeguard Screening Form for classification of projects (SSF)
[IDBDocs36260293](#)

ABBREVIATIONS

PFM	Public financial management
AWP	Annual work plan
CAPTAC-DR	Centro Regional de Asistencia Técnica para Centroamérica, Panamá y la República Dominicana [Regional Technical Assistance Center for Central America, Panama, and the Dominican Republic]
CGR	Contraloría General de la República [Office of the Comptroller General of the Republic]
CIAT	Inter-American Center of Tax Administrations
CUT	Cuenta Única del Tesoro [Single Treasury Account]
DIPRENA	Dirección de Presupuesto de la Nación [National Budget Directorate]
DGI	Dirección General de Ingresos [General Revenue Directorate]
DGT	Dirección General de Tesorería [General Treasury Directorate]
DNC	Dirección Nacional de Contabilidad [National Accounting Directorate]
DPI	Dirección de Programación de Inversiones [Investment Programming Directorate]
DPL	Development policy loan (World Bank)
IMF	International Monetary Fund
ITBMS	Impuesto de Transacciones de Bienes Corporales Muebles y la Prestación de Servicios [Goods and services sales tax]
LRSF	Ley de Responsabilidad Social Fiscal [Social and Fiscal Responsibility Law]
MEF	Ministry of Economy and Finance
MFMP	Marco Fiscal de Mediano Plazo [Medium-term Fiscal Framework]
NFPS	Nonfinancial public sector
OC	Ordinary Capital
PCA	Panama Canal Authority
PCU	Program coordination unit
PEG	Plan Estratégico de Gobierno [Government Strategic Plan]
PEP	Plan de Ejecución Plurianual [Multiyear Implementation Plan]
PMR	Program monitoring report
PQI	Plan Quinquenal de Inversiones [Five-year Investment Plan]
SIAFPA	Sistema Integrado de Administración Financiera de Panamá [Integrated Financial Management System of Panama]
SIAFPA-Pro	SIAFPA project management module
SIGADE	Sistema de Gestión y Análisis de la Deuda [Debt Management and Analysis System]
SINIP	Sistema Nacional de Inversión Pública [National Public Investment System]
SIPRES	Sistema de Formulación Presupuestaria [Budget Formulation System]
TAT	Tribunal Administrativo Tributario [Tax Administration Tribunal]

PROJECT SUMMARY

PANAMA PROGRAM TO STRENGTHEN FISCAL MANAGEMENT (PN-L1066)

Financial Terms and Conditions				
Borrower: Republic of Panama			Amortization period:	20 years
			Grace period:	36 months
Executing agency: Republic of Panama, acting through its Ministry of Economy and Finance (MEF)			Disbursement period:	36 months
Source	Amount US\$	%	Interest rate:	LIBOR-based
IDB (Ordinary Capital)	50 million	91	Credit fee:	*
Local	5 million	9	Inspection and supervision fee:	*
Total	55 million	100	Currency:	U.S. dollars from the Single Currency Facility
Project at a Glance				
Program objective. The general objective of the program is to contribute to increasing public investment to the levels required by the Government Strategic Plan, through a sustainable increase in tax revenues and improvements in the efficiency of public expenditure management.				
Description. The program has four components: Component I – Modernization of tax administration (US\$17 million); Component II – Consolidation of public expenditure management (US\$18.1 million); Component III – Strengthening of public financial management (US\$7.5 million); and Component IV – Technological integration (US\$4.3 million).				
Special contractual conditions precedent to the first disbursement: (i) Evidence that the program coordination unit (PCU) has been established, and its general coordinator and monitoring and evaluation, procurement, and administrative/financial specialists appointed (see paragraph 3.4); and (ii) evidence that the advisory committee has been created (see paragraph 3.3).				
Exceptions to Bank policy: None.				
Special considerations: The program includes recognition of retroactive expenditures for up to US\$5 million of the Bank financing (see paragraph 3.8).				
Project consistent with country strategy: Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>				
Project qualifies as: SEQ <input type="checkbox"/> PTI <input type="checkbox"/> Sector <input type="checkbox"/> Geographic <input type="checkbox"/> Headcount <input type="checkbox"/>				

* The credit fee and inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with the applicable provisions of the Bank's policy on lending rate methodology for Ordinary Capital loans. In no case will the credit fee exceed 0.75% or the inspection and supervision fee 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. DESCRIPTION AND RESULTS MONITORING

A. Background, problem addressed, rationale

1. Macroeconomic performance

- 1.1 Panama's macroeconomic performance in recent years has been strong, and it is one of the fastest growing emerging economies. Between 2003 and 2010 its economy grew at an annual average of more than 6% in real terms, slowing only briefly in 2009 due to the international financial crisis. Gross domestic product (GDP) per capita in Panama grew from US\$4,470 in 2004 to US\$7,712 in 2010, establishing a sustained growth trend. In 2010, the economy posted a growth rate near 7.5%, and similar rates are expected in the coming years. In 2010, inflation reached 3% annually, and 2.7% to 2.8% inflation is forecast for 2011. The unemployment rate fell to 6.5% in 2010, and stands at a historically low level. In recent years, the Government of Panama strengthened its fiscal policy framework with the aim of: (i) enhancing the sustainability of its public finances; (ii) ensuring macroeconomic and financial stability; (iii) improving expenditure quality and efficiency; (iv) increasing the effectiveness of budgetary management; and (v) gradually reducing public debt as a percentage of GDP.
- 1.2 Management of public finances has been prudent. After the nonfinancial public sector (NFPS) reported surpluses of 0.5%, 3.5%, and 0.4% of GDP in 2006-2008, respectively, thanks to the strong economic performance, the government set a commitment to limit the NFPS deficit to 1% of GDP, and (net) public debt to no more than 40% of GDP. The Fiscal and Social Responsibility Law of 2008 (known by its Spanish-language acronym, LRSF) was enacted with that in mind, and then amended in June 2009 to create leeway for countercyclical policies in response to the global crisis. Because of this, in 2009 and 2010 the government was allowed a fiscal deficit of 2.5% and 2% of GDP, respectively, returning to the 1% of GDP ceiling in 2011. Despite the fiscal leeway, the deficit reported was just 1% and 1.9% of GDP in 2009 and 2010, respectively. In December 2010, the deficit ceiling for 2011 was temporarily raised to 3%, in order to finance emergency works in response to torrential rains, but with the commitment to return to the 1% of GDP ceiling in 2013.
- 1.3 Within the framework of the LRSF, the Government of Panama formulated a Government Strategic Plan (PEG), which, in turn, contains a Medium-term Fiscal Framework (MFMP) and a Five-year Investment Plan (PQI) for the 2010-2014 period. To finance the 2010-2014 PQI, which calls for US\$13.6 billion, the government implemented two tax reforms to increase tax revenues by 2.5% of GDP on a permanent basis. The 2010-2014 PQI proposes doubling public investment over the 2005-2009 period, bringing it to 10% to 12% of GDP.

Table 1.1: Main macrofiscal indicators, 2006-2011

INDICATOR	2006	2007	2008	2009	2010p	2011e
Real GDP growth (%)	8.5	12.1	10.7	2.4	7.5	6.3
Nominal GDP (US\$ millions)	17,137	19,794	23,184	24,575	26,728	28,412
Inflation (annual)	2.2	6.4	6.8	1.9	3.0	2.7
Total public revenue (% GDP)	26.8	29.7	29.2	27.4	27.8	29.0
Total public expenditures (% GDP)	25.6	25.0	26.7	27.9	29.8	30.9
External debt (% GDP)	40.5	37.4	32.7	36.5	38.5	39.5

Source: Office of the Comptroller General of the Republic and International Monetary Fund. p: preliminary; e: estimate.

2. Fiscal trends

- 1.4 **Tax administration.** As of late 2009, Panama had total fiscal revenue equivalent to over 20% of GDP, including net revenue from the Panama Canal worth 3% of GDP and income from contributions to the pension system of 6% of GDP. Nonetheless, the country had one of the lowest tax revenue levels in Latin America, at just 10.7% of GDP. This reflects a tax structure that has fallen behind trends in the rest of the Americas and weaknesses in tax administration processes.
- 1.5 **Public investment.** Between 2004 and 2009, public sector investment expenditure grew sharply (from 3.1% to 7.1% of GDP), thanks to higher tax revenues and earnings from the Panama Canal, which together accounted for some 56% of total public sector revenues. In that period, total public sector revenues grew by 3.5% of GDP. Nonetheless, to sustain the level of public investment on the order of 7% to 8% of GDP, and possibly increase it, the authorities detected the need to increase the tax burden and to strengthen tax administration.

Table 1.2: Public sector fiscal indicators, 2006- 2011 (% of GDP)

	2006	2007	2008	2009	2010p	2011e
Tax revenues	10.3	10.6	10.5	10.7	11.7	12.5
Income from the Panama Canal	3.5	4.3	3.0	3.2	2.8	3.4
Primary expenditure	17.0	16.0	15.4	15.8	16.1	16.2
NFPS fiscal balance (excl. PCA*)	0.5	3.4	0.4	-1.0	-1.9	-2.3
NFPS primary balance (excl. PCA)	4.8	6.9	3.5	1.8	2.0	1.7

Source: International Monetary Fund. p: preliminary ; e: estimate. * Panama Canal Authority

3. Fiscal management challenges

- 1.6 One of the main challenges of fiscal management for the Government of Panama is to increase public investment to the levels proposed in the PEG while remaining in compliance with the LRSF. The purpose of increased public investment is to address the country's sharp geographical disparities and disparities in economic opportunities. The main obstacles to increased public investment are: (i) Panama

has one of the lowest levels of tax revenues in the region, just 11.7% in 2010, due to low tax rates and weak tax administration; (ii) neither budgetary management nor the monitoring and evaluation of public investment programs has a results-driven culture; (iii) there are weaknesses in the financial and accounting management of public resources; and (iv) information generated by the information technology systems used for fiscal management is of poor quality. A description of the leading causes that aggravate the aforementioned problems is given below, divided into sections by area of public financial management.

- 1.7 **Tax administration.** A joint diagnostic assessment of tax administration in Panama¹ by the Inter-American Center of Tax Administrations (CIAT), the Regional Technical Assistance Center for Central America, Panama, and the Dominican Republic (CAPTAC-DR), and the Bank ([see electronic link](#)) concluded that, despite certain progress, the General Revenue Directorate (DGI) is still constrained by: (i) structural deficiencies in its organizational model; (ii) shortcomings in the effective structuring of managerial processes (oversight, collection, and taxpayer services); (iii) limited use of information technology tools, business intelligence, and risk criteria in tax collection; and (iv) weak mechanism to promote tax compliance.
- 1.8 **Investment programming.** With Bank support, the Ministry of Economy and Finance (MEF) recently strengthened the technical role of investment programming functions. This notwithstanding, investment programming still has the following shortcomings: (i) the information technology tool of the National Public Investment System (SINIP) has been developed only at the level of the project bank; (ii) no system exists of outcome indicators for monitoring and evaluating PQI outcomes at the central and sector levels; and (iii) the SINIP is still not integrated into the SIPRES-Web budget information system, which limits the capacity to evaluate the investment budget.
- 1.9 **Budget system.** In Panama the budget is structured mainly by program, but has the following weaknesses: (i) lack of information on objectives and targets, and not explicitly linked to the 2010-2014 PEG; (ii) five-year budgetary projections are not broken down, systematically prepared, or publicly accessible; there is still no year-by-year MFMP that would make it possible to formulate a multiyear budget; and (iii) lack of a system of budgetary performance indicators and budget allocation mechanisms to foster efficiency and effectiveness in the management of NFPS institutions.

¹ *Informe-Diagnóstico de la Dirección General de Ingresos de Panamá* [Report/diagnostic assessment of the General Revenue Directorate of Panama], CAPTAC/CIAT/IDB (June 2010).

Table 1.1 Simplified diagnostic assessment of fiscal management in Panama (PN-L1066)

Target area	Problem detected	Causes	Proposed intervention	Results indicators
Tax administration	Panama has one of the lowest levels of tax revenue collected in Latin America and the Caribbean: 10.7% of GDP.	Structural deficiencies in its organizational model; shortcomings in the structuring of managerial processes; limited use of information technology tools, business intelligence, and risk criteria in tax collection; weak tax compliance.	Modernization of tax administration (US\$17 million): Reform of the operational and physical organization of the DGI; improvement of tax management; technological modernization; strengthening of tax compliance.	Revenue generated through the Large Taxpayer Unit. ITBMS revenue collected as a percentage of GDP (Bank's country strategy with Panama 2010-2014).
Public expenditure management	No results-based management in the monitoring and evaluation of public investment and the budget.	Investment programming: The National Public Investment System (SINIP) is only a project bank; no system for monitoring and evaluating public investment. Budget: No objectives and targets, and not explicitly linked to the 2010-2014 PEG; no budgetary performance indicators.	Consolidation of public expenditure management (US\$18.1 million): Strengthening of monitoring and evaluation of investment programming and multiyear results-based budgeting.	Percentage of central government institutions using the SINIP (Bank's country strategy with Panama 2010-2014). Percentage executed of the annual target of the NFPS public investment budget (capital expenditure).
Financial management systems	Weaknesses in the financial and accounting management of public resources, and low-quality information.	Treasury: No legal framework for the Single Treasury Account (CUT); the NFPS ministries and agencies manage more than 6,000 bank accounts. Accounting: No conceptual model for the Integrated Financial Management System of Panama (SIAFPA).	Strengthening of public financial management (US\$7.5 million): Creation of the CUT; training on accounting rules and draft law on public financial management (PFM); strengthening of MEF financial programming and fiduciary management of projects.	Percentage of central government institutions governed by the CUT. Percentage of central government institutions using the SIAFPA-Web online platform.

**Table 1.1 Simplified diagnostic assessment of fiscal management in Panama
(PN-L1066)**

Target area	Problem detected	Causes	Proposed intervention	Results indicators
Information and communication technologies	The existing information and communication technology (ICT) platforms supporting public financial management (PFM) are obsolete.	There are 14 systems with 5 distinct platforms. They employ different designs, standards, and methodologies, and are not integrated.	Technological integration (US\$4.3 million): Upgrade of the MEF technological platform to support PFM; Adaptation of the MEF's technological standards.	Number of MEF information technology interconnection and telecommunication systems to support PFM integrated.

- 1.10 **Treasury and Single Treasury Account (CUT).** At present, the bodies responsible for the government's cash management have the following weaknesses: (i) the General Treasury Directorate (DGT) does not have the installed capacity to automatically manage the central government's daily cash balances or to more effectively perform its payment functions; (ii) the DGT has limited ability to efficiently invest the treasury's cash on hand; (iii) in terms of the payment function, the Office of the Comptroller General of the Republic (CGR) has still not transferred functions that by law correspond to the MEF; (iv) the Treasury and the CUT are lacking an adequate legal framework; and (v) the ministries and decentralized agencies of the NFPS manage, at their discretion and without the Treasury's oversight, more than 6,000 bank accounts.
- 1.11 **Government accounting.** In 2009-2010 the National Accounting Directorate (DNC) reviewed the accounting processes of the public administration, and audited the information technology systems of the Integrated Financial Management System of Panama (SIAFPA). It concluded that: (i) the telecommunications and database platforms currently in place to run their applications were obsolete; (ii) a module was needed for financial/accounting monitoring of public projects (SIAFPA project management module (SIAFPA-Pro), which was later created in 2010); and (iii) a conceptual model needed to be defined for accounting integration and for effective connectivity of the following modules: revenue (e-Tax), SINIP, budget (SIPRES-Web), Treasury and CUT, and the Debt Management and Analysis System (SIGADE).

4. Rationale

- 1.12 To consolidate fiscal management within the framework of the LRSF mandates, and to increase the level of public investment, it will be necessary to strengthen the tools for efficient financial management in Panama's public sector. This will involve introducing improvements in tax administration, as well as designing and implementing more efficient and transparent mechanisms for administering public expenditures.
- 1.13 This program will support the Government of Panama's efforts to lock in gains made in fiscal management through the adoption of modern public financial management processes. The program will implement several policy measures agreed upon under policy-based loan 2473/OC-PN, approved on 1 December 2010. The objective of that loan is to support policy measures that improve and consolidate fiscal policy, public financial management, and tax equity, with a view to strengthening fiscal sustainability in the medium and long terms.

B. The Bank's country and sector strategy

- 1.14 One of the priorities of the Bank's country strategy with Panama for 2010-2014 is to strengthen public finances. Support to that area has two strategic objectives: (i) higher tax revenue, and (ii) more efficient public expenditure. The expected strategy outcomes in the revenue area are: (i) higher tax revenue; (ii) greater international tax transparency and coordination; and (iii) modernization of tax

administration. The expected outcomes in the area of public expenditures are: (i) use of public investment and multiyear results-based budgets (PPR) systems; (ii) consolidation of integrated financial management systems; and (iii) use of the CUT.

- 1.15 As indicated in the Bank's support strategy, in order to finance and execute the 2010-2014 PQI and comply with the LRSF, the Government of Panama must strengthen its public finances, which it will do by increasing tax revenue collection and improving the systems for public investment programming, budgetary management, treasury operations, public debt, and financial management. This will enable the country to remain on the path of fiscal sustainability it has followed over the last decade.
- 1.16 Since 2002, the Bank has supported the MEF's efforts to strengthen public financial management. The Bank approved and implemented with the MEF the Program to Strengthen and Modernize Economic and Fiscal Management, Phase II (loan 1430/OC-PN, 2003-2009), which laid the groundwork for an integrated and modern public financial management system. That program supported the Panamanian government in increasing the tax yield through the use of an alternative method for calculating income tax (CAIR), creation of a project bank, compilation of seven sector public investment plans, automatic budget formulation using the SIPRES-Web module, strengthening of SIGADE and development of the SIAFPA public credit module, automation of payments to government suppliers through electronic bank transfers, and creation of the National Customs Authority, among other outcomes and outputs. For all these components, the program financed procedures, procurement of equipment, and training.
- 1.17 In 2008 and 2009, the Bank advised the Panamanian government on the implementing regulations for the LRSF, putting into practice the key principles of fiscal policy established in the law. Since 2009, the Bank has also provided the MEF with ongoing advisory support on tax policy options and, more recently, on the design for reengineering tax administration. The Bank's support in this area focused specifically on the reform of the goods and services sales tax (ITBMS) and the income tax (ISR), implementation of international taxation measures, and creation of the Tax Administrative Tribunal (TAT). More recently, support was provided for administrative modernization of the DGI, particularly in creating the Large Taxpayer Unit, and in the area of oversight, with the implementation of fiscal printers.²
- 1.18 This ongoing policy dialogue with the Panamanian government led progressively to the structuring of the present investment loan to modernize the areas of revenue and public expenditure.

² Fiscal printers are electronic devices that directly control the invoicing of retail commerce by recording each sale on magnetic media accessible only to the tax administration for audit purposes.

C. Objectives

- 1.19 The general objective of the program is to contribute to increasing public investment to the levels required by the Government Strategic Plan (PEG), through a sustainable increase in tax revenues and improvements in the efficiency of public expenditure management.

D. Components and costs

- 1.20 The program has four components, each with its respective subcomponents and outputs. All components seek to strengthen the institutional capacity of the MEF by updating its legal frameworks, modernizing its administrative and business processes, upgrading information technology systems for operational support, and modernizing its physical and technological structures. To this end, the program will include training activities, consulting services, procurements of equipment and information technology systems, procurement of other equipment and support materials, and facility improvements.

1.21 Component I. Modernization of tax administration (US\$17 million)

- a. **Subcomponent 1.1. Reform of the operational and physical organization of the DGI.** This subcomponent will finance: (i) a new organizational model, (ii) a new institutional planning model, (iii) a new human resources model, (iv) remodeling and equipment for the taxpayer services office, and (v) physical improvements and equipment for the DGI operations departments.
- b. **Subcomponent 1.2. Improvement of tax management processes.** This subcomponent will finance: (i) strengthening of services for large taxpayers; (ii) implementation of the international taxation area; and (iii) strengthening of the tax collection, enforcement, and collection process.
- c. **Subcomponent 1.3. Modernization of technological and tax infrastructure.** This subcomponent will finance: (i) the restructuring of the DGI information technology unit; (ii) development and execution of an information technology business plan; (iii) adjustment of the tax management system and redesign of the DGI's website; (iv) strengthening of information technology services and database quality control; (v) creation of a unit to implement and determine security rules and software; (vi) improvements in the functionality of the e-Tax system; (vii) implementation of electronic payments for tax obligations via Web; and (viii) adaptation of the telecommunications and database platforms.
- d. **Subcomponent 1.4. Strengthening of tax compliance mechanisms.** This subcomponent will finance implementation of the Tax Administrative Tribunal (TAT).

1.22 **Component II. Consolidation of public expenditure management (US\$18.1 million)**

- a. **Subcomponent 2.1. Investment programming and multiyear budgetary management.** This subcomponent will finance: (i) improvement of monitoring and evaluation procedures at the Investment Programming Directorate (DPI) and sector institutions; (ii) capacity-building of planning units to formulate and monitor sector public investment plans; (iii) implementation of software to support investment programming at ministries and their provincial offices; (iv) implementation of a training program on quality control of georeferencing in investment projects; (v) creation of the Public Investment Evaluation Unit; and (vi) strengthening of public investment management at the municipal level.
- b. **Subcomponent 2.2. Multiyear results-based budget.** This subcomponent will finance: (i) launching of the Budget Monitoring and Evaluation Unit; (ii) implementation of multiyear results-based budgeting processes; (iii) introduction of monitoring of budget management indicators in SIPRES-Web; (iv) capacity-building of the Information Technology Unit to report on budget management performance; (v) implementation of advisory services and training program for entities and sectors; (vi) implementation of a training program for monitoring budget management performance; and (vii) formulation of a new legal framework for budget management.

1.23 **Component III. Strengthening of public financial management (US\$7.5 million)**

- a. **Subcomponent 3.1. Single Treasury Account (CUT).** This subcomponent will finance: (i) implementation of a program to establish the procedures for treasury operations and the CUT; and (ii) vetting of checking accounts and automation of bank transfers to central government agencies.
- b. **Subcomponent 3.2. Integrated financial management system.** This subcomponent will finance: (i) a training program on financial and accounting management for public investment projects; (ii) a certification program on international public sector accounting regulations, and continuity of the SIAFPA; and (iii) formulation of a law on integrated financial management.
- c. **Subcomponent 3.3. Financial programming.** This subcomponent will finance: (i) strengthening of the MEF financial programming unit; and (ii) establishment of a project administrative management office at the MEF.

1.24 **Component IV. Technological integration (US\$4.3 million)**

- a. **Subcomponent 4.1. Upgrade of the MEF technological platform to support public financial management (PFM).** This subcomponent will finance: (i) upgrade of management tools, network monitoring, and security and antivirus software for the PFM subsystems; (ii) installation of the Blade server to facilitate PFM; (iii) implementation of the “zero paper” project; and (iv) upgrade of

telecommunications and logistics infrastructure in the information technology area supporting the PFM.

b. Subcomponent 4.2. Adaptation of the MEF's technological standards.

This subcomponent will finance: (i) implementation of the comprehensive information technology security model; (ii) regularization of the status of licenses for applications installed on workstations; and (iii) training program on networks, security, project management, programming, and database management.

Table 1.3 Indicative costs by component (US\$000s)

		IDB	MEF	Total
Component I:	Modernization of tax administration	17,000	1,700	18,700
	Tax administration	16,500	1,650	18,150
	Tax Administration Tribunal (TAT)	500	50	550
Component II:	Consolidation of public expenditure management	18,100	1,810	19,910
	Investment programming	13,000	1,300	14,300
	Budget	5,100	510	5,610
Component III:	Strengthening of public financial management	7,500	750	8,250
	Treasury and CUT	4,700	470	5,390
	SIAFPA	1,800	180	1,980
	Financial programming	1,000	100	1,100
Component IV:	Technological integration	4,300	430	4,730
	MEF technological platform	3,300	330	3,630
	MEF technological standards	1,000	100	1,100
	Administration and audit	2,890	310	3,200
	Evaluation	210	0	210
Total		50,000	5,000	55,000

E. Key results indicators

- 1.25 The expected impact is increased levels of public investment in line with the Government Strategic Plan (PEG). The principal expected outcomes of the program are higher tax revenues and more efficient public expenditure management. A breakdown of the outcomes and outputs of this program is given in the Results Matrix (see Annex II). The Results Matrix indicators are consistent with those in the results matrix of the Bank's country strategy with Panama 2010-2014 and in the 2011 country programming document for Panama.

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instrument

- 2.1 The total amount of the program is US\$55 million, with Bank financing of US\$50 million to be disbursed over a period of 36 months, and a local counterpart

contribution of US\$5 million from the Government of Panama. The program is compatible with the institutional capacity developed by the Ministry of Economy and Finance (MEF) to execute this type of operation in two previous programs with the Bank. The modality agreed upon for this program is the investment loan.

B. Coordination with other financing and donor agencies

- 2.2 This program supports the government's strategy to consolidate its fiscal policy by increasing the NFPS primary surplus, and increasing investment levels in order to reduce poverty with the support of multilateral agencies. The program is also aligned with the technical recommendations of the International Monetary Fund (IMF), through the Regional Technical Assistance Center for Central America, Panama, and the Dominican Republic (CAPTAC-DR), to strengthen the tools for implementation of the LRSF. It also complements a development policy loan (DPL) from the World Bank. As part of preparation of this program, the public expenditure and financial accountability (PEFA) assessment is being coordinated with the World Bank. In the context of strengthening fiscal policy, the World Bank approved a development policy loan (First Programmatic Fiscal Management and Efficiency of Expenditures Development Policy Loan, P123255), which reinforces policy measures that complement this operation. In addition, this operation complements a US\$55 million World Bank investment loan (Enhanced Public Sector Efficiency Technical Assistance Loan, P121492), which will finance work to strengthen multiyear results-based budgetary management (including investment programming, the MFMP, and the budget), a new model for public accounting and external control, socioeconomic statistics, and the strengthening of public procurement systems. To ensure complementarity, the activities of the two investment loans were designed jointly with the MEF to be implemented by a single program coordination unit (see Annex III). The IDB will coordinate activities with the World Bank in the areas of monitoring and evaluation of investment programming, budgetary management, and government accounting; in this last area, the Bank's participation will be limited to staff training. The two loans were designed in parallel and discussed with the MEF in order to avoid an overlapping of activities and redundancy of resources.

C. Environmental and social safeguard risks

- 2.3 Since the program involves institutional strengthening activities, no environmental or social risks are directly associated with it. Based on the results of the Safeguards Policy Filter Report and the Screening Form, this operation has been classified as category "C" ([see electronic link](#)).

D. Other key issues and risks

- 2.4 The three main risks of this operation have been analyzed with the Panamanian authorities. They are: (i) the difficulties due to complexity that the government will face in achieving the PFM modernization objectives. This risk will be mitigated by a thorough review of the Results Matrix indicators during the program startup mission, and ongoing supervision with monitoring of those indicators; (ii) delays or

inconsistencies in the information on flows of program funds. This risk will be mitigated with the establishment of an information technology system with the SIAFPA-Pro module software as its hub, which will report the program's financial and physical progress online in a manner compatible with the Bank's system (program monitoring report (PMR)); and (iii) delays in procurements or insufficient technical capability to conduct them. To mitigate this risk, technical coordinators will be dedicated exclusively to the preparation of terms of reference for the consulting services. In addition, a training program will be carried out for staff members of beneficiary MEF directorates, who will work with the full-time fiduciary experts of the program coordination unit (PCU).

- 2.5 The formulation of the Government Strategic Plan (PEG), the Medium-term Fiscal Framework (MFMP), and the Five-year Investment Plan (PQI) for the 2010-2014 period testify to the government's determination to establish the basic parameters that will guide the MEF-led public financial management (PFM). The government has achieved consensus on the need to significantly increase public investment. This will only be achieved if a performance framework is established that effectively regulates the budgetary, financial, and fiduciary transactions of the public sector.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

- 3.1 **Borrower and executing agency.** The borrower will be the Republic of Panama, acting through the Ministry of Economy and Finance (MEF) as executing agency. Four bodies will be involved in program coordination and execution: (i) one that will focus on policy and strategy coordination for decision-making, made up of the vice ministers of economy and of finance; (ii) an advisory committee that will oversee program consistency and compatibility; (iii) a coordination body—the program coordination unit (PCU)—that will be responsible for all aspects of implementation, and serve as liaison between the first level of the MEF and the Bank; and (iv) point people at the technical level of the components and subcomponents into which the program is organized, in the MEF's line departments.

B. Program execution and administration

- 3.2 **Policy and strategy coordination.** Program policy and strategy coordination will be the responsibility of the vice ministers of economy and of finance who, together, will serve as the liaison for: (i) ensuring leadership and continuity in the modernization and institutional strengthening process; (ii) ensuring attainment of the program's objectives and scope as well as the proper use of resources; and (iii) validating the process to implement the activities of the multiyear implementation plan (PEP), as well as to achieve the outcomes set out in the program Result Matrix. In order to assess the general performance of the program,

the vice ministers will meet at least once a year to approve the PEP submitted by the PCU, and to hold an annual review meeting.

- 3.3 **Advisory committee.** In order to support the consistency and compatibility of the different activities set out in the PEP, the program will have an advisory committee made up of the heads of the following eight directorates of the Ministry of Economy and Finance: Revenues, Investment Programming, Budget, Treasury, National Accounting, Public Policy, Technology and Information, and Administration/Finance. The advisory committee will be responsible for steering the PCU's work program and for reporting the progress made in achieving program outcomes and outputs to the two vice ministers, represented on this committee by the directors of Public Credit and Investment Programming. **Evidence that the advisory committee has been created will be a condition precedent to the first disbursement.**
- 3.4 **Internal coordination (PCU).** The existing program coordination unit (PCU) under the Vice Ministry of Economy, responsible for execution of the Support to Results-based Management operation (PRODEV, ATN/OC-11401-PN), will be strengthened to implement the PEP approved by the Vice Ministers of Economy and of Finance. This same PCU satisfactorily executed the Program to Strengthen and Modernize Economic and Fiscal Management, Phase II (loan 1430/OC-PN), and engages ministry career staff and contractors to support specific aspects of program execution. In addition, the PCU will facilitate the coordination and consistency of activities planned for the different MEF departments under each component. On an annual basis, each line department will inform the PCU of its budget requirements in this regard for the following fiscal period. Each line department will also report to the PCU on program execution on a six-monthly basis. **Evidence that the PCU has been established, and its general coordinator and monitoring and evaluation, procurement, and administrative/financial specialists appointed, will be a condition precedent to the first disbursement.**
- 3.5 **Component execution.** The execution, administration, and supervision of the activities under each component and/or subcomponent will be the responsibility of the relevant MEF line department. A technical coordinator will be appointed in each MEF line department to assume that responsibility; this person will report directly to the relevant director.
- 3.6 **Accounting and financial management, audit, and disbursements.** The PCU will be responsible for program accounting and financial management, in coordination with the MEF's Administration and Finance Department. The SIAFPA-Pro module will be used to make program payments and keep program records. In addition, the PCU will be responsible for submitting the program's audited financial statements to the Bank annually within 120 days after the close of each fiscal year or the date of the last disbursement at program end. These financial statements will be audited by a firm of independent auditors acceptable to the Bank, based on terms of reference previously approved by the Bank, in accordance with Operational Policy OP-273-1 and the document "Guidelines for Financial Reports

and External Audit of Operations Financed by the Inter-American Development Bank.” Disbursements will be made under the advance of funds modality, in accordance with the program’s actual liquidity needs, reimbursements for payments made, or direct payments to suppliers, pursuant to Operational Policy OP-273-1.

3.7 **Procurement.** Program procurements will be conducted in accordance with the Bank’s policies for the procurement of works and goods financed by the Bank (document GN-2349-9) and its policies for the selection and contracting of consultants financed by the Bank (document GN-2350-9). International competitive bidding will be applicable when the cost of the good is equal to or greater than US\$250,000, and when the cost of works is equal to or greater than US\$3 million. National competitive bidding will be applicable when the cost of the good is equal to or greater than US\$50,000, and when the cost of works is equal to or greater than US\$250,000. The shopping method will be applicable when the cost of the good is less than US\$50,000, and when the cost of works is less than US\$250,000. In the case of consulting services, the short list of consultants may comprise solely national consultants when the cost is equal to or less than US\$100,000. The Inter-American Center of Tax Administrations (CIAT) may be contracted directly for the “Modernization of tax administration” component, in continuation of the satisfactory services this specialized agency has provided to the General Revenue Directorate (DGI) in tax administration processes.

3.8 **Advance contracting and retroactive financing.** The Bank may recognize up to US\$5 million against the Bank loan proceeds, and up to US\$500,000 against the local counterpart contribution, in expenditures incurred by the borrower under Component I and Subcomponent 2.1. To be recognized, expenditures must have been incurred no more than 18 months prior to the date of approval of this operation by the Board of Executive Directors, and subsequent to the approval date of the project profile (28 October 2010). The objective of the retroactive expenditures to be recognized is to advance critical activities in the areas of remodeling facilities, advisory services on systems, equipment, and training related to tax administration, and the procurement of software and training for the SINIP. These activities are part of an accelerated timetable for changes in these areas of the MEF, so that it can meet its 2011 operational targets. They will involve contracting for individual consultants, consulting firms, and works, as well as procurement of software and equipment. These procedures are consistent with the policy governing retroactive expenditures (Operational Policy OP-504).

C. **Summary of arrangements for monitoring results**

3.9 The annual outcome and output indicators described for each component in the Results Matrix, and reflected in the program monitoring report (PMR) will be used to measure the program’s progress and assess achievement of its objectives. The indicators, aligned with the Bank’s country strategy with Panama for 2010-2014, focus on the modernization of tax administration, public expenditure management, integrated financial management, and technological integration. Administration missions will be made to verify progress on these indicators, during which risks that

may affect achievement of program outcomes will also be updated. A detailed description of the monitoring and evaluation arrangements for program outcomes is provided in [required electronic link 3](#).

- 3.10 **Monitoring system.** The SIAFPA-Pro module developed by the MEF will be used to ensure ongoing and effective monitoring of actions over the course of the program. In addition, the PCU will monitor the program on a day-to-day basis, through: (i) the PEP, which includes the procurement plan and links outputs to the results matrix indicators; (ii) the annual work plan (AWP); and (iii) six-monthly progress reports based on the results matrix indicators and the PMR, to be delivered within 60 calendar days after the close of each six-month period, or on a date agreed upon with the Bank. The indicators for this evaluation will be based on the results matrix. The values of the indicators compiled by the PCU will provide input for the program PMR, with special attention to how the physical and financial progress of the program's specific outputs determine the "earned value" of the program as a whole.
- 3.11 **Midterm and final evaluations.** The midterm evaluation will be delivered to the Bank within 90 days after the date on which 50% of the loan resources have been disbursed, or after 18 months of execution, whichever occurs first. The final evaluation report, which will serve as an input for the project completion report, will be delivered within 90 days after the date on which 90% of the loan resources have been disbursed. These evaluations will be performed by consulting firms and financed with loan proceeds.
- 3.12 **Evaluation methodology.** Given the nature of the program, which focuses on institutional changes in financial management at the MEF, it is difficult to generate precise benefit flows for a traditional economic cost-benefit analysis at the program preparation stage without delaying approval of the program. However, a cost-effectiveness analysis that was performed identified significant financial benefits, including higher tax revenue and lower transaction costs in public financial management. To supplement the initial cost-effectiveness evaluation, an economic cost-benefit analysis will be performed for each component after program completion, identifying hedonic attributes and using contingent valuation methods, based on existing literature on the economic analysis of the impact of institutional reform. This evaluation is reflected in the program's monitoring and evaluation plan.

Development Effectiveness Matrix			
Summary			
I. Strategic Alignment			
1. IDB Strategic Development Objectives	Aligned		
Lending Program	The intervention contributes to the lending program for small and vulnerable countries.		
Regional Development Goals	The intervention contributes to the goal of ratio of actual to potential tax revenue.		
Bank Output Contribution (as defined in Results Framework of IDB-9)	The intervention contributes to the public financial systems implemented or upgraded (budgeted, treasury, accounting, debt, and revenues).		
2. Country Strategy Development Objectives	Aligned		
Country Strategy Results Matrix	GN-2596	The intervention contributes to improve the collection rates and to modernize the tax administration; as well as to improve management and efficiency of public spending.	
Country Program Results Matrix	GN-2617	Te intervention is included in the 2011 Country Program Document.	
Relevance of this project to country development challenges (If not aligned to country strategy or country program)			
II. Development Outcomes - Evaluability	Evaluable	Weight	Maximum Score
	6,9		10
3. Evidence-based Assessment & Solution	5,0	25%	1
4. Ex ante Economic Analysis	10,0	25%	1
5. Monitoring and Evaluation	5,2	25%	1
6. Risks & Mitigation Monitoring Matrix	7,5	25%	1
Overall risks rate = magnitude of risks*likelihood	Low		
Environmental & social risk classification	C		
III. IDB's Role - Additionality			
The project relies on the use of country systems (VPC/PDP criteria)	yes	The project relies on the use of SIAFPAPRO and Panama Compras.	
The project uses another country system different from the ones above for implementing the program			
The IDB's involvement promotes improvements of the intended beneficiaries and/or public sector entity in the following dimensions:			
Gender Equality			
Labor			
Environment			
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project	yes	PN-T1024 Results-Based Public Management (PRODEV).	
The ex-post impact evaluation of the project will produce evidence to close knowledge gaps in the sector that were identified in the project document and/or in the evaluation plan.			

The program presents ample evidence of the problems currently affecting Panama's capacity to increase public investment: (i) high levels of tax evasion and tax expenditures, which greatly affect the level of revenues available for investment; and (ii) the inefficiencies imbedded in the administration of public resources, most notably the lack of a Single Treasury Account and the lack of comprehensive fiscal information that can inform decisions. The diagnosis needs further analysis of the magnitudes of the factors impacting on the problem. The interventions proposed are those tested in other countries as those that can most effectively address the problems presented. The creation of a Large Contributor Unit, improved methodologies for control, electronic tax payments, and increased automatization of receipts are interventions used across the region to address evasion, tax debt, and efficiency in tax collection. On the expenditure side, the consolidation of accounts, improved system for tracking investments, the interface of the investment and budget systems; and improved timeliness of budget information have all proven to be effective in reducing inefficiencies, costs and the availability of relevant data for decision-making.

The vertical logic of the project would benefit from intermediate results for each component, as the results of the project are all indicators of the Country Strategy leading to the large jumps between input, product, result and impact. Intermediate results per component would clearly measure the extent to which the products affected a change. This is necessary to ensure that the logic of the intervention is clear. Not all indicators are SMART.

The project used an ex-ante cost-effectiveness analysis for two subcomponents: (i) the improved controls and audit of the DGI; and (ii) the establishment of the Single Treasury Account, which yields increased interests collected from available liquidity. These two subcomponents' costs are then compared to an alternative without the project in which the following interventions are done: (i) reduce evasion ITBMS by way of reduction of tax expenditures, (ii) reduce the number of days the treasury resources sit idle in bank accounts of executing agencies, by way of administrative improvements to bidding processes of government. These alternative yield lower economic benefits (greater costs) and therefore the project interventions are more effective. The project proposes to do an ex-post cost-benefit analysis for which resources have been allocated.

The project has no high risks associated with it. The mid level risks are related to the implementation of the coordination unit, and these are mitigated by involvement of the project team leader in the process of establishing and contracting the staff for the unit. The indicators for the monitoring of the mitigation measures are not all SMART.

RESULTS MATRIX

Program objective	To contribute to increasing public investment to the levels required by the Government Strategic Plan (PEG) through sustainable increases in tax revenues and improvements in the efficiency of public expenditure management.		
Project impact indicator	Base line	End target	Observations
Five-year investment increased to the levels required by the Government Strategic Plan (PEG).	1. 2009: US\$7.5 billion for 5-year investment (2004-2009)	2. 2014: US\$13.6 billion for 5-year investment (2010-2014)	Source: Report on budget execution and report of the Medium-term Fiscal Framework (MFMP) of the MEF (quarterly)
Outcome indicator	Base line	End target	Observations
General Revenue Directorate (DGI) revenues generated through the Large Taxpayers Unit	2010: US\$393.4 million	2014: At least US\$800 million	Source: DGI reports to the program advisory committee (half-yearly)
ITBMS revenue collected as a percentage of GDP (Bank's country strategy with Panama 2010-2014)	2009: 2% (MEF)	3% or more	Source: DGI reports to the program advisory committee (half-yearly)
Percentage executed of the annual target of the NFPS public investment budget (capital expenditure)	2010: 80%.	2014: 95%	Source: Reports of the Investment Programming Directorate (DPI) to the program advisory committee (half-yearly)
Percentage of central government institutions using the SINIP (Bank's country strategy with Panama 2010-2014)	2010: 0% (MEF)	2014: 90%	Source: DPI reports to the program advisory committee (half-yearly)
Percentage of central government institutions governed by the CUT	2010: 0%	2014: 100%	Source: Reports of the General Treasury Directorate (DGT) to the program advisory committee (half-yearly)
Percentage of central government institutions using the SIAFPA-Web online	2010: 0%	2014: 80%	Source: Reports of the National Accounting Directorate (DNC)

platform			reports to the program advisory committee (half-yearly)
Number of MEF information technology interconnection and telecommunication systems to support PFM integrated.	2010: 0	2014: 10	Source: Reports of the Information Technology Directorate (DTI) reports to the program advisory committee (half-yearly)

Component 1 – Modernization of tax administration	Base line (2010)	Targets					Observations
		2011	2012	2013	2014	End	
Output indicators							
Principal functions introduced in the DGI’s Large Taxpayers Unit	0	1 (Filer monitoring)	1 (Arrears monitoring)	1 (Noncompliance audit)	1 (Objective risk enforcement)	4	Source: DGI reports to the program advisory committee (half-yearly)
International Taxation Unit (ICU) created and operating	0	0	1	0	1	1	Source: DGI reports to the program advisory committee (half-yearly)
New fiscal printers operating and audited	0	1,000	2,000	2,000	2,000	7,000	Source: DGI reports to the program advisory committee (half-yearly)
Methodology for estimating tax expenditure introduced	0	0	1	0	0	1	Source: DGI reports to the program advisory committee (half-yearly)
Auditors of the Large Taxpayers Unit receive training in advanced corporate audit methods	0	0	75	75	50	200	Source: DGI reports to the program advisory committee (half-yearly)

Component 2 – Consolidation of public expenditure management	Base line (2010)	Target					Observations
		2011	2012	2013	2014	End	
Output indicators							
Main functions strengthened in the Monitoring and Evaluation (Unit for investments (SINIP)	0	1 formulation	1 (ex ante review)	1 (monitoring)	1 (ex post review)	4	Source: DPI reports to the program advisory committee (half-yearly)
Five main functions introduced in the Budget Management Unit of the National Budget Directorate (DIPRENA).	1	1 formulation	2 monitoring and reassignment	2 Consolidation and evaluation	0	5	Source: DIPRENA reports to the program advisory committee (half-yearly)
Draft preliminary bill prepared for the Budget Act	0	0	1	0	0	1	Source: DIPRENA reports to the program advisory committee (half-yearly)
Sector institutions have implemented the system of indicators for monitoring and evaluating their investment programs	0	1	3	5	0	9	Source: DPI reports to the program advisory committee (half-yearly)
Public employees receive training in georeferencing, program and project monitoring and evaluation, using the tools of SINIP and SIPRES-Web	20	300	300	380	0	1000	Source: DPI and DIPRENA reports to the program advisory committee (half-yearly)

Component 3 – Strengthening of public financial management	Base line (2010)	Target					Observations
		2011	2012	2013	2014	(End)	
Output indicators							
Central government checking accounts vetted and automated under the CUT	0	0	4,200 (90% of central government)	1,300 (10% of central government and 100% of autonomous entities and public enterprises)	1,000	6,500	Source: DGT reports to the program advisory committee (half-yearly)
Central government staff receive training in financial and accounting management of public investment projects	0	0	250	250	0	500	Source: DNC reports to the program advisory committee (half-yearly)
Central government staff receive training in international public sector accounting standards (IPSAS)	0	0	400	400	0	800	Source: DNC reports to the program advisory committee (half-yearly)
Draft preliminary bill prepared for the law on financial management	0	0	1	0	0	1	Source: DNC reports to the program advisory committee (half-yearly)
Financial Programming Unit created and in full operation in coordination with seven MEF directorates	0	0	1	0	0	1	Source: Reports of the Planning and Budget Directorate (DPP) to the program advisory committee (half-yearly)
Fiduciary Project Management Unit created and in operation	0	0	1	0	0	1	Source: DPP reports to the program advisory committee (half-yearly)

Component 4 – Technological integration	Base line (2010)	Target					Observations
		2011	2012	2013	2014	(End)	
Output indicators							
Standards of interoperability for the information technology (firewall, antivirus, spam, storage, data warehouse, etc.) and telecommunications (telephony, data, images, etc.) systems identified by the Information Technology Directorate (DTI) to support public financial management (PFM).	0	1	5	4	0	10	Source: DTI reports the program advisory committee (half-yearly)
Information and communication technology support systems/services for PFM fully operational.	2	2	5	1	0	10	Source: DTI reports to the program advisory committee (half-yearly)

FIDUCIARY AGREEMENTS AND REQUIREMENTS

Country: Panama
Project: PN-L1066
Name: Program to Strengthen Fiscal Management
Executing agency: Ministry of Economy and Finance (MEF)
Prepared by: Karina Díaz Briones, Procurement Specialist (PDP/CPN); and Juan Carlos Dugand, Financial Management Specialist (PDP/CPN)

I. EXECUTIVE SUMMARY

- 1.1 The evaluation of fiduciary management was performed through visits by the fiduciary experts at the Bank's Country Office in Panama, on the occasion of the preparation of this loan, and the evaluation of the MEF's performance as executing agency of loan 1430/OC-PN, which concluded in 2009, and of technical cooperation operation ATN/OC-11401-PN, now in progress.
- 1.2. In terms of procurement, although Panama has made significant progress, successive amendments are being made in the legislation with a view to expanding the scope of bidding processes for better value, and to increasing flexibility in the use of direct contracting. The government is beginning implementation of a World Bank-financed program to strengthen the public procurement system (Project ID: P121492). In terms of the use of the system, the Bank accepts the use of the information portal and the framework agreement for procurements valued at less than US\$50,000 under a pilot project conducted with the World Bank. In terms of country financial systems, a project module is being implemented for the Integrated Financial Management System of Panama (SIAFPA), which will be piloted in project PN-L1066.
- 1.3 The project does not include financing from other multilateral agencies, but the MEF has negotiated another loan with the World Bank that includes complementary activities in support of the MEF. Therefore, it is relevant to consider the need for effective coordination between the two projects. This is reflected in the creation of the strengthened program coordination unit (PCU), which will handle the day-to-day administration of the two operations. Standardized financial reports were agreed upon with the World Bank, to be used for monitoring both projects. The SIAFPA project module (SIAFPA-Pro) will also be used as a pilot project.

II. FIDUCIARY CONTEXT OF THE EXECUTING AGENCY

- 2.1 The MEF has two vice ministries (Economy and Finance), comprising various directorates that operate very independently. For this reason, execution will require that effective coordination be promoted within the MEF. The project will involve the following directorates: Dirección Nacional de Ingresos [General Revenue Directorate] (DNI); Dirección General de Tesorería [General Treasury Directorate] (DGT); Dirección Nacional de Contabilidad [National Accounting Directorate] (DNC); Dirección de Programación de Inversiones [Investment

- Programming Directorate] (DPI); Dirección de Presupuesto de la Nación [National Budget Directorate] (DIPRENA); Dirección de Políticas Públicas [Public Policy Directorate] (DPP); Dirección de Tecnología de la Información [Information Technology Directorate] (DTI). Each directorate has its own budget, and will conduct activities independently of the others. Some changes will therefore have to be made in the SIAFPA project module so that it can administer this type of project.
- 2.3 In executing prior projects with the IDB, the MEF used resource administrators, who, on behalf of the MEF, handled the procurements and payments required by the project. For this new program, the MEF will directly handle the procurements and payments necessary for execution.
- 2.4 By Executive Decree 9, issued in January 2011, the Project Administrative Management Directorate (DGA-MEF) was created within the Vice Ministry of Economy. Its purpose is to support the administration of own resources, or resources from international lenders, for the administrative management of procurements and payments. Notwithstanding this, in February 2011, the MEF requested, in a letter to the World Bank with a copy to the IDB, that the implementation arrangement for the two projects be unified, with the structure indicated (see electronic link: [IDBDocs35823989](#)).
- 2.5 As can be seen, the execution structure does not include the recently created DGA-MEF. Therefore, agreement was reached among the MEF, the IDB, and the World Bank that once the directorate was ready to begin operations, the necessary adjustments would be made to fully align the execution arrangements. The understanding is that, during implementation of the two projects, the PCU will be gradually scaled down until the DGA-MEF takes over all its fiduciary functions, preferably before the conclusion of the IDB and World Bank projects.

III. ASSESSMENT OF FIDUCIARY RISK AND MITIGATION ACTIONS

- 3.1 The following fiduciary risks were identified: (i) delays or inconsistencies in the information on flows of program funds. This risk will be mitigated with the establishment of an information technology system with the SIAFPA-Pro module software as its hub, which will report the program's financial and physical progress on a monthly basis. The risk is considered moderate because, in any event, to be able to make the payments for the program, it will be necessary to use all the budgetary and accounting controls of SIAFPA; and (ii) delays in procurements or insufficient technical capability to conduct them. To mitigate this risk, technical coordinators will be dedicated exclusively to the preparation of the terms of reference for the consulting services. In addition, a procurement specialist will be engaged to support the PCU in preparation of the procurement plan for the first 18 months of execution, and training sessions on the Procurement Plan Execution System (SEPA) will be held for staff members of beneficiary MEF directorates, who will work with the full-time fiduciary experts of the PCU.
- 3.2 Given the experience gained with executing earlier projects and the modus operandi of the different departments of the MEF, along with the parallel

execution of the World Bank-financed project, achieving a suitable level of coordination is a challenge. Therefore, at the start-up workshop and in the IDB's semiannual administration missions with the program, execution of the initial version of the risk mitigation plan proposed and accepted by the MEF will be expressly discussed.

IV. POINTS TO BE ADDRESSED IN THE SPECIAL PROVISIONS OF THE CONTRACTS

- 4.1 In order to streamline the contract negotiation by the project team, and especially the LEG, the agreements and requirements that should be considered in the special stipulations are as follows: (i) procurements shall be governed by the Bank policies in documents GN-2349-9 and GN-2350-9; (ii) retroactive expenditures will be recognized for up to the equivalent of 20% of the loan amount; (iii) thresholds for international advertising for works, goods, nonconsulting services, and consulting services are consistent with country thresholds established by PDP; (iv) mixed arrangement of ex ante and ex post review of procurements; (v) the initial procurement plan will be prepared together with the Bank; once the operation is approved, the first procurement plan will be prepared using the Procurement Plan Execution System (SEPA); (vi) annual audited financial statements will be required on an annual basis, as well as an annual professional opinion by auditors regarding the effectiveness of the internal controls in place for project execution; (vii) in the event that the existing parity between the balboa and the dollar is eliminated, the exchange rate should be agreed to by the Bank and the borrower; and (viii) special contractual clauses: (a) evidence that the PCU has been established, and its general coordinator and monitoring and evaluation, procurement, and administrative/financial specialists appointed; and (b) evidence that the program advisory committee has been created.

V. AGREEMENTS AND REQUIREMENTS FOR PROCUREMENTS

- 5.1 The fiduciary agreements and requirements relating to procurements establish the provisions that shall apply for all procurements foreseen for the program; they will be executed by the procurement area of the program coordination unit.
- 5.2 Works, goods, and nonconsulting services will be procured in accordance with GN 2349-9, of April 2011; the selection and contracting of consulting firms will follow GN 2350-9 of April 2011.

A. Execution of procurements

- a. **Procurement of works, goods, and nonconsulting services:** International competitive bidding (ICB) will use the standard bidding documents issued by the Bank. National competitive bidding (NCB) and shopping will be done in accordance with the models defined by the Bank for this operation. The review of the technical specifications of procurements during the preparation of selection processes will be the responsibility of the program's sector specialist. A specific description of program procurements can be found in the program procurement plan (see electronic link).

- **Procurement of information technology systems:** The program will finance the elaboration of information technology systems; to this end, the standard bidding documents for the procurement of information technology products and services will be used.
- b. **Selection and contracting of consultants:** Contracts for the program's consulting services will be executed using the standard call for proposals issued by the Bank.
 - **Selection of individual consultants:** This will be based on the consultants' qualifications for the job at hand, and will involve comparison of the qualifications of at least three candidates;
 - **Training:** Although training will be financed through courses existing in the market, the design of training for the consulting firms to be contracted is also included.
- c. **Recurrent costs:** Financing for per diems and rental of premises has been provided for. In addition, the program will finance the positions of the staff of the program coordination unit.
- d. **Advance procurement:** The Bank may recognize up to US\$5 million against the Bank loan proceeds, and up to US\$500,000 against the local counterpart contribution, in expenditures incurred by the borrower under Component I and Subcomponent 2.1. To be recognized, expenditures must have been incurred no more than 18 months prior to the date of approval of this operation by the Board of Executive Directors, and subsequent to the approval date of the project profile (28 October 2010). The objective of the retroactive expenditures to be recognized is to advance critical activities in the areas of remodeling facilities, advisory services on systems, equipment, and training related to tax administration, and the procurement of software and training for the SINIP. These activities are part of an accelerated timetable for changes in these areas of the MEF, so that it can meet its 2011 operational targets. They will involve contracting for individual consultants, consulting firms, and works, as well as procurement of software and equipment. These procedures are consistent with the policy governing retroactive expenditures (Operational Policy OP-272).
- e. **Domestic preference:** Not applicable.
- f. **Others:** The following will be financed: internships, dissemination plans, courses and workshops, support materials, and dissemination. Training also includes the contracting of courses existing in the market. For each case, a plan will be prepared with the items of expenditure and respective budget, and shopping will be used as appropriate. In addition, the program will finance the purchase and/or rental of physical premises.

B. Table of thresholds (US\$000)

Works			Goods ¹			Consulting services	
International competitive bidding	National competitive bidding	Shopping	International competitive bidding	National competitive bidding	Shopping	International advertising consulting services	Short list 100% national
More than or equal to US\$3,000,000	More than US\$250,000 and less than US\$3,000,000	Less than US\$250,000	More than or equal to US\$250,000	More than US\$50,000 and less than US\$250,000	Less than US\$50,000	More than US\$200,000	Less than or equal to US\$200,000

Ex post review thresholds

Works and goods	Consulting services
Shopping	Consulting firms for amounts below US\$100,000 Individual consultants for amounts below US\$50,000

C. Principal procurements

MAIN BANK-FINANCED PROCUREMENTS

Description of expected procurement	Estimated amount (US\$000)	Selection method
Goods		
Install a new information technology and telecommunications platform	3,000	ICB
Purchase or rent, furnish and equip building for the operations departments	4,000	ICB
Remodel and equip the tax administration building	1,000	ICB
Information technology equipment for the different areas of the MEF	2,000	ICB, NCB, or shopping
Nonconsulting services		
Various trainings, workshops, and internships	3,300	Shopping
Consulting firms		
Contract different consulting firms for organizational development and restructuring of the different departments of the MEF, as well as to design information technology platforms aligned with these restructurings	12,000	QCBS
Contract consulting firms to introduce the online banking system for the treasury and the CUT	600	QCBS
Design internship arrangements and training	100	QCBS
Individual consultants		
National and individual consultants to support the program and/or prepare specific products for departments involved in the program	4,300	IICQ, NICQ

D. Review of procurements

- 5.3 The thresholds established for ex post review have been set in accordance with the executing agency's fiduciary capacity for execution, and may be modified by the Bank to the degree that said capacity changes. Only the processes covered in the procurement plan will be subject to ex post review; all direct contracting will be reviewed ex ante. Ex post reviews will be performed every 12 months, pursuant to the program's supervision plan. Ex post review reports will include at least one physical inspection visit, chosen from among the procurement processes subject to ex post review.

¹ Includes nonconsulting services.

E. Special provisions (Not applicable)

F. Records and files

- 5.4 The safekeeping and management of contracting files is the responsibility of the program coordinator, who will appoint a staff person specifically for this activity.

VI. FINANCIAL MANAGEMENT

A. Programming and budget

- 6.1 The MEF has the responsibility of formulating and overseeing the budget. According to the law creating the MEF (Law 95-1998) and its administrative regulations, the MEF is to submit a proposed budget before 31 July of each term to the National Assembly, which is responsible for its approval and for any increases in same. The budget is annual, and includes all public sector investments, revenues, and outlays. Because the draft budget is prepared so early, many modifications are made to it, so it loses its validity as a planning instrument. All payments by the public sector are recorded in the budget. The budget for the 2011 fiscal year does not include budget items for the program, but transfers between budget items amounting to around US\$1 million are envisaged to finance some initial program activities, which may be considered for reimbursement chargeable to the IDB loan (see Chapter IV, section b).

B. Accounting and information systems

- 6.2 The SIAFPA was adopted in 2000 as the official system for recording accounting and budget information, and includes budgetary, treasury, accounting, and public debt modules. Recently a projects module has been developed that will be piloted with the financial management of the program. In addition, the SIAFPA's information technology platform will be updated under the World Bank-financed project.
- 6.3 Accounting will be governed by the rules issued by the Office of the Comptroller General of the Republic (CGR), which are on an accrual basis, but they are not aligned with international public sector accounting standards (IPSAS). Audited financial statements of the program will be required on an annual basis.

C. Disbursements and cash flow

- 6.4 In Panama, the concept of single treasury account (CUT) is still not in effect. Fixed parity exists between the dollar and the balboa, which is used as the account unit and is limited to the emission of fractional currency in denominations lower than US\$1. Therefore, Panama freely uses United States paper currency as a means of payment.
- 6.5 The IDB will make disbursements in accordance with the modality of advances to a bank account used exclusively for management of such resources, based on the funds needed according to the financial plan. The SIAFPA project module is being adapted so that program payments can be made directly by the Treasury through online bank transfers, instead of using checks. All payments by the different departments will be channeled through the program coordination unit.

D. Internal control and internal audit

- 6.6 Although the MEF has an internal audit office, the internal control system is weak since the Office of the Comptroller General of the Republic (CGR) exercises prior fiscal oversight, and internal control is essentially based on that work. External auditors will verify, on an annual basis, the effectiveness of internal controls implemented for program execution.

E. External control and reports

- 6.7 The CGR exercises prior oversight, and therefore lacks the independence needed to perform the external control of the program. It is necessary for an independent audit firm to audit the program's financial statements, and to issue a professional opinion on the effectiveness of the internal controls implemented for execution. The terms of reference will be agreed upon with the Bank. The estimated cost of the audit is US\$60,000 per year, for a total of US\$240,000 for the four years of program execution, and will be financed with loan proceeds. These costs are expressly reflected in the program's monitoring and evaluation plan.

F. Financial oversight plan

- 6.8 Financial oversight will focus on verifying the internal controls that make it possible to reasonably conclude that the resources are being used for the stated purposes of the program, and on verifying the correct operation of the SIAFPA project module. Supporting documentation for disbursements will be reviewed ex post at least once a year.