

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

## **PARAGUAY**

### **PUBLIC MANAGEMENT MODERNIZATION PROGRAM**

**(PR-L1043)**

### **LOAN PROPOSAL**

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## CONTENTS

### PROJECT SUMMARY

I.	DESCRIPTION AND MONITORING OF RESULTS .....	1
A.	General framework and background .....	1
B.	Problems to be mitigated by the program .....	2
C.	Program challenges, strategy, coordination, and rationale .....	3
D.	Objectives and components .....	5
E.	Key indicators of the results matrix.....	9
II.	FINANCING STRUCTURE AND RISKS .....	10
A.	Financing and contractual conditions.....	10
B.	Risks and mitigating measures .....	10
III.	IMPLEMENTATION AND MANAGEMENT PLAN.....	11
A.	Summary of agreements reached for implementation.....	11
B.	Summary of agreements reached for monitoring performance .....	11
IV.	MATRIX OF CONDITIONS FOR DISBURSEMENT .....	11

## ANNEXES

Annex I	Summary Development Effectiveness Matrix (DEM)
Annex II	Policy matrix

ELECTRONIC LINKS (REQUIRED)	
1	Policy Letter <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1975374">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1975374</a>
2	Means of verification <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963638">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963638</a>
3	Results matrix <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1958305">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1958305</a>

ELECTRONIC LINKS (OPTIONAL)	
4	Assessment of democratic governance (ICF/ICS, December 2008) <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963979">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963979</a>
5	World Bank PDL report ( <i>approved 5 May 2009</i> ) <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963982">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963982</a>
6	Sixth Final Review of the Stand-By Arrangement (International Monetary Fund – IMF – August 2008) <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963992">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963992</a>
7	Strengthening budget preparation and debt management (IMF Report, 27 February 2009) <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963996">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1963996</a>
8	IMF report on the March 2009 mission (Article IV) ( <i>approved 1 May 2009</i> ) <a href="http://www.imf.org/external/spanish/np/sec/pr/2009/pr0980s.htm">http://www.imf.org/external/spanish/np/sec/pr/2009/pr0980s.htm</a>
9	Project Completion Report (PCR) PROFOMAF I <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1424438">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1424438</a>
10	PROFOMAF II preparation and execution reports <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1864168">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1864168</a>
11	Integrated Fiduciary Assessment - IFA (2008) <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1964011">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1964011</a>
12	Matrix of the government plan to be supported by the PDPL series (World Bank) <a href="http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1964015">http://ops/idbdocs/docsMain/getdoc.asp?docnumber=1964015</a>

## APPENDICES

Proposed resolution

## **ABBREVIATIONS**

BCP	Central Bank of Paraguay
CUT	Single Treasury Account
DNCP	National Public Procurement Division
GDP	Gross national product
IDB	Inter-American Development Bank
IMF	International Monetary Fund
OC	Ordinary Capital
PDL	Policy development loan
PEU	Program executing unit
PPPs	Public-private partnership investments
PROPEF	Project Preparation and Execution Facility
SbE	Electronic Dutch auction
SIAF	Integrated Financial Management System
SINARH	National Human Resources Administration System
SNIP	National Public Investment System
STP	Planning Technical Secretariat, Office of the President of the Republic

## PROJECT SUMMARY

### PARAGUAY PUBLIC MANAGEMENT MODERNIZATION PROGRAM (PR-L1043)

Financial Terms and Conditions				
<b>Borrower:</b> Republic of Paraguay			Amortization period:	20 years
<b>Executing agency:</b> Ministry of Finance			Grace period:	5 years
			Disbursement period:	24 months
<b>Source</b>	<b>Amount (US\$)</b>	<b>%</b>	Inspection and supervision fee:	*
IDB (Ordinary Capital)	100,000,000	100	Interest rate	LIBOR/fixed**
Local	-	-	Credit fee:	*
Total	100,000,000	100	Currency:	U.S. dollar from the Single Currency Facility
Project at a glance				
<b>Project objective:</b> <p>The purpose of the program is to improve government capacity to analyze, execute, and monitor public spending and administrative management, in order to improve the quality, efficiency, and transparency of public expenditure management. The program is divided into five components: (i) macroeconomic stability, (ii) public policy coordination and efficiency, (iii) public expenditure management systems, (iv) public investment system, and (v) central government human resources administration.</p>				
<b>Special contractual conditions:</b> <p>See Matrix of Conditions in Chapter IV. ( 4.1)</p>				
<b>Exceptions to Bank policies:</b> <p>No exceptions to Bank policies are envisaged.</p>				
<b>Project consistent with country strategy:</b> Yes [ X ]      No [ ]				
<b>Project qualifies as:</b> SEQ [ ]      PTI [ ]      Sector [ ]      Geographic [ ]      Headcount [ ]				

\* 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.

\*\* The adjustable rate, which is to be discontinued on 1 July 2009, will be replaced with LIBOR/fixed.

## I. DESCRIPTION AND MONITORING OF RESULTS

### A. General framework and background

- 1.1 The Ministry of Finance of Paraguay requested the Bank's support for undertaking the design and introduction of a set of policy reforms to improve public expenditure management as a priority preventive action for coping with the possible effects of the international financial crisis both this year and next. The present loan operation is the first of a **programmatic series** to support policy reform, which will be made up of two contractually independent and technically linked loans, as per document CS-3633.
- 1.2 **Macroeconomic considerations.** Implementation of policy reforms requires a stable macroeconomic framework compatible with the program's objectives. The amounts proposed are consistent with Ministry of Finance estimates on resource requirements in 2009 and 2010, and will make it possible to support a monetary and fiscal policy mix that will be sustainable over the medium term. However, an unexpected surge in spending, followed by a decline in tax revenues, could endanger the fiscal balance.
- 1.3 According to the Central Bank of Paraguay (BCP), the country's **gross domestic product** (GDP) grew by an estimated 5.8% in 2008, with average annual growth of 4.6% between 2003 and 2008. Per capita GDP was up by 2.8% on average, to US\$1,556. Cumulative inflation in 2008 was 7.5%, slightly higher than the 6% recorded in 2007, even though the cumulative annual rate was 13.4% in July 2008; since then it has been in a downtrend.
- 1.4 A **current account** deficit of 1.4% of GDP was recorded in 2008, after four years of positive performance, due primarily to the effect of high fuel prices on the value of imports in the first three quarters of the year. The result was a negative trade balance of US\$1.034 billion that was more than offset by capital inflows of US\$402 million. Accordingly, **net international reserves** in December stood at US\$2.864 billion, or 4.3 months of imports, a 16.3% improvement from 2007.
- 1.5 With regard to **fiscal performance**, the government's central administration generated a surplus of 1,831 billion guaranis (Gs) to December 2008, the result of a 17.6% nominal increase in total revenues and 6.6% in spending compared to 2007. In addition, real income accumulated in 12 months increased by 9.42%, while real expenditures contracted by 1% compared to the previous December. Thus, at year-end 2008, fiscal performance of the central administration had posted a **surplus** equivalent to 2.6% of GDP.
- 1.6 Over the past five years, **tax revenues** have been growing by around 2% of GDP, to 12.4% of GDP in 2008, reaching an accumulated Gs8.656 billion in that year (28.2% higher than the same period in 2007). VAT revenues make up 52.1% of tax receipts (30% more than collected by the previous December), while revenues from receipts and profits account for 18.2% (28.1% more than the same period in 2007). In addition, by December 2008, total foreign exchange earnings of the Itaipú and

Yacyretá Hydroelectric Plants were US\$423.6 million, a US\$16.2 million improvement from 2007.

- 1.7 In 2008, **central administration expenditures** showed an 18.1% increase in spending on personnel, and a 13.9% contraction in capital expenditures, associated with the electoral process. The composition of spending remained stable from 2004 to 2007, average personnel expenditures accounted for around 7.3% of GDP, and capital expenditures contracted from 4.2% of GDP in 2006 to 2.9% in 2008.
- 1.8 Consolidated **public sector investment** followed the same pattern, falling to 3.7% of GDP in 2008. For its part, private-sector investment during the period averaged 14.2% of GDP, bringing total investment to an average 18.7% during the 2004-2008 period. The ratio of tax receipts to recurrent expenses moved from 92% in 2004 to 96.5% in 2008, meaning that 96.5% of recurrent expenses are financed by tax revenues.

## **B. Problems to be mitigated by the program**

- 1.9 In recent years, significant efforts have been made in Paraguay to improve central administration fiscal discipline through different actions to modernize public expenditure management. Some of the outcomes of these efforts include technical improvements in the budget process within the financial planning and cash management areas, and in budget accounting, with the introduction of a commitment stage. Further progress has been made with the Integrated Financial Management System (SIAF), and in the area of public procurement. These improvements have helped improve fiscal discipline in the central administration, increase tax revenues, and improve efficiency in procurements, all of which have helped restore the country's fiscal stability, demonstrated by five consecutive years of fiscal surplus.<sup>1</sup>
- 1.10 Although major progress has been made, certain aspects still need to be addressed to increase the efficiency and effectiveness of public expenditure management. These include the principal challenges identified in the 2008 PEFA (Public Expenditure and Financial Accountability) of the Integrated Fiduciary Assessment (IFA), which refer to the need for improvements in budget process efficiency, greater fiscal transparency, and more effective controls. What these challenges have in common is limited institutional capacity in the public sector, which underscores the need to modernize the different public expenditure management processes and systems in a gradual and consistent fashion. Below are some of the **main problems** the program will address:
- 1.11 Public policy coordination and efficiency: (i) Excessive institutional fragmentation and proliferation of Secretariats and other organizational units, which hinder

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<sup>1</sup> Fiscal management modernization in Paraguay has been receiving Bank support for many years, and substantial progress was made with the Fiscal Management Strengthening and Modernization Program I (**PROFOMAF-I**, Loan 1253/OC-PR), approved in 2000 and completed in 2008 with very positive outcomes.

interinstitutional coordination and the processes to formulate, execute, and evaluate policies and public spending; and (ii) insufficient analysis and control mechanisms for the planning, budgeting, execution, and evaluation of public spending, mainly for the social and economic sectors.<sup>2</sup>

- 1.12 Public expenditure management systems: (i) Limited regulatory capacity for efficient management of financial administration, particularly for treasury and cash management in the execution of aggregate public resources; and (ii) government procurement system in the early stages of upgrading bidding process efficiency and effectiveness.
- 1.13 Public investment system: (i) Limited planning, prioritization, and alignment with government programs, and limited monitoring of public investment projects, leading to under-execution of programs; (ii) insufficient capacity to manage investment projects, and little integration between the planning, design, execution, and evaluation stages; and (iii) excessive sector fragmentation of roles and regulations for the promotion, management, and articulation of public-private investment partnerships, and insufficient capacity for economic analysis and monitoring of such projects.
- 1.14 Central government personnel administration: (i) insufficient controls in personnel management; (ii) few posts in program executing units (PEUs) filled by permanent staff; high turnover, low level of commitment, and limited project implementation capacity; and (iii) insufficient statistics for monitoring aggregated personnel expenditures in the central government.<sup>3</sup>

### **C. Program challenges, strategy, coordination, and rationale**

- 1.15 This program was designed to mitigate the problems described above, with the overarching purpose of continuing to help maintain the fiscal balance, and to provide the civil service in Paraguay with the tools to upgrade the efficiency, quality, and transparency of public spending.
- 1.16 **Rationale.** The programmatic format is justified because the program includes short-term policy actions that will be strengthened by other medium- and long-term ones. It is also justified because it will contribute to improving transparency, control, and the capacity for public expenditure management as part of a strategy to give continuity and sustainability to actions being taken by the Paraguayan government with Bank support in recent years.

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<sup>2</sup> The Bank's 2008 Governance Study found that there was no effective body coordinating State policies, and that the STP did not fulfill that role entirely. With a few exceptions of coordination with multilateral aid agencies or the private sector, or because of the need to meet international objectives, there has been no serious effort to structure State agencies in order to improve coordination between them. This lack of coordination is also evident in the area of social policy.

<sup>3</sup> The 2008 IFA concluded that the reliability of the staff roster is undermined by incomplete records and the absence of a personnel data base. Changes introduced in the roster and the nominal roster tend to take considerably longer than three months, making retroactive adjustments common. Although controls do exist, they are insufficient to ensure completeness of the data.



- 1.17 The program **strategy** is to help the Paraguayan government address the economic slowdown stemming mainly from the recent drought and the effects of the international financial crisis. The Executive Branch is planning to submit to Congress an **Economic Recovery Plan** that includes this program and other specific policies to maintain macroeconomic stability and mitigate adverse impacts. Specifically, the program strategy calls for promoting certain policy reforms in coordination with and supplementing other reforms supported by the principal multilateral and bilateral agencies active in the country.
- 1.18 In addition, it intends to take advantage of, leverage, supplement, and consolidate the progress made in public expenditure management begun with PROFOMAF I (loan 1253/OC-PR, completed successfully in 2008), and the Preinvestment Program (1143/OC-PR, currently in progress), which were continued with PROFOMAF II (2014/BL-PR approved in 2008 and launched in 2009 with PROPEF 1964/OC-PR), and the program to professionalize the civil service (1776/OC-PR, in execution since 2008 with PROPEF 1775/OC-PR).
- 1.19 Some lessons learned from other Bank programmatic programs with Paraguay were incorporated, including: (i) using easily measurable indicators and defining baselines; (ii) strengthening project executing units, as per disbursement condition 5.2; and (iii) not limiting Bank support to approving the reforms, but also helping the government to implement them through institutional strengthening actions, process review, information systems, training, and others.
- 1.20 The program was coordinated with the **World Bank**, which, on 5 May 2009, approved a Policy Development Loan (PDL) for a first US\$100 million operation in a programmatic series. The PDL includes commitments such as making certain changes in tax policy, improving the effectiveness of internal financial controls (strengthening the independence of the Office of the General Auditor of the Executive Branch), more effective supervision of government enterprises (creation of the Government Enterprise Council), and maintaining the proportion of social spending in the total budget (around 49% in the central administration). The Andean Development Corporation (CAF) and the **Japan International Cooperation Agency (JICA)** were also requested by the Ministry of Finance for additional contributions of unrestricted resources.
- 1.21 The **International Monetary Fund (IMF)** led two missions to Paraguay in early 2009, the first to provide technical assistance to the Ministry of Finance in relation to the budget process and debt management; the second to review Article IV, which was approved on 1 May 2009. The assessments and recommendations from these two IMF missions were taken into consideration in analyzing policy options for the present program.
- 1.22 The **Bank's country strategy with Paraguay** for the 2009-2013 period proposes that the Bank's action focus on the following: (i) strengthening the administrative management of the State to enable its institutions to design better policies, deliver better public services, and provide legal guarantees for people and investments;

(ii) strengthening the development of production activities and competitiveness by deepening the financial sector, providing infrastructure, and expanding markets; and (iii) expanding opportunities for the low-income population through coordinated support for the development of rural communities, an expansion of early childhood care coverage, improvements in the coverage and quality of basic education, and expansion of the population covered by conditional cash transfers. The present operation will contribute to strengthening the administrative management of the State, the first area the Bank's action will target.

#### **D. Objectives and components**

- 1.23 The **objective of this programmatic series** is to improve government capacity for analysis, execution, and monitoring of public expenditures and administrative management, thus helping to upgrade the quality, efficiency, and transparency of public expenditure management.
- 1.24 Implementation of the reforms called for requires a stable macroeconomic framework consistent with the objectives of the programmatic series and the projections of the Ministry of Finance (<http://www.hacienda.gov.py>). The amounts proposed are consistent with Ministry of Finance estimates on resource needs in 2009 and 2010, and support the financial requirements of 2009 envisioned in the Bank's programming.
- 1.25 In preparing the present operation, all technically and politically viable and suitable policy options were analyzed for each scenario to determine. On this basis, the matrix of disbursement conditions (triggers) was finally established for the single tranche of this first operation of the programmatic series, as was a preliminary identification of the policy commitments estimated for 2010.
- 1.26 The program's five components are described below, as are the activities being carried out by the government to meet all the commitments in 2009. The final commitments of this first operation, as conditions for disbursement, are set out in the table of paragraph 4.1. The impacts of the programmatic series are shown in the **Results Matrix** (Link #4).
- 1.27 **Component I. Macroeconomic stability.** Objective: Maintain a stable macroeconomic policy framework consistent with program objectives and the guidelines set out in the sector policy letter. The Economic Reactivation Plan the Executive Branch intends to submit to Congress includes specific policies for maintaining macroeconomic stability and for mitigating the impact of the international financial crisis. Moreover, in recent years, Paraguay has fulfilled its commitments with the IMF, including the last review, in August 2008, of a Stand-By Arrangement, and approval of Article IV.
- 1.28 For the past five years, the country's macroeconomic situation has been stable (as reported in the Bank's recently validated Independent Macroeconomic Assessment – IMA), with an economic growth rate exceeding the historical pattern, fiscal and current account surpluses, and a reduction in public borrowing

to under 20% of GDP. With a strengthened financial system, the country is in a position to weather the international financial crisis.

- 1.29 **Component II. Public policy coordination and efficiency.** General objective: Reduce organizational overlap and promote greater coordination and efficiency in the formulation, execution, and evaluation of public policies for the principal categories of public spending, with special emphasis on the economic and social sectors. The specific objective of this component in this **first operation** is to help the government design policy proposals for modernizing structures and procedures, including the development of legal standards for organizational reform in the economic and social areas, and strategies and actions for improving the control procedures and systems of the conditional cash transfer program (referred to in Paraguay as “cash transfers with shared responsibility”).
- 1.30 The strategy chosen for organizational reform is to focus on the Ministry of Finance and the social area. This will make it possible to maximize policy viability since several proposals are already being discussed and have been prioritized by the government. Amendment of Law 109, which sets out the structure of the Ministry of Finance and is a condition for disbursement, will help transform the Ministry of Finance into a Ministry of Economy, which will later absorb the Technical Planning Secretariat (STP).<sup>4</sup>
- 1.31 The policy option selected for the social sector is to begin reorganizing the sector, and to improve control procedures and systems for cash transfers with shared responsibility. The aim is to increase the number of beneficiary families in the TEKOPORA Program from 18,000 to 120,000, as proposed by the government. (TEKOPORA is the largest government program providing cash transfers with shared responsibility.)
- 1.32 With regard to the organizational rearrangement of the social sector, the Ministry of Finance’s Social Economy Unit (UES) made an inventory of current structures, as well as their regulatory and legal aspects. The strategy is to begin working with those created by decree or ruling. With regard to cash transfers with shared responsibility, the PEU is working to create a single list of TEKOPORA beneficiaries, and to have payments be made through the banking system. This will be detailed in a specific action plan, and will include other aspects needed to modernize the control procedures and systems of TEKOPORA’s integrated information system, such as beneficiary eligibility, compliance with shared responsibility, financial control, and monitoring of processes, outputs, and impact assessment. Also, the World Bank has reached agreement with the government on

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<sup>4</sup> Consideration was given to the possibility of introducing a wide range of organizational reforms. This was not deemed technically and politically viable, however, as there are very few assessments and proposals, and other types of legal, political, and cultural hurdles exist.

additional commitments for protecting social spending, and other policies associated with this program.<sup>5</sup>

- 1.33 **Component III. Public expenditure management systems.** General objective: Promote increased integration, quality, and transparency of the information coming from cross-cutting systems that support public expenditure management, including treasury, accounting, budget, and public procurement; promoting improvements in their level of development, coverage, and access; and strengthening information security. The specific objective of this component in this **first operation** is to promote better cash management by the government, adjust the legal framework for financial management with a view to strengthening public expenditure efficiency, and to further modernize the country's public procurement system.
- 1.34 To improve cash management by the Treasury Department, the Ministry of Finance is following best international practices to implement a **Single Treasury Account** (CUT) that will provide for more effective use and control of the financial resources of the central administration. While there has been an increase in recent years in the number of independent bank accounts opened at the Central Bank of Paraguay (BCP) associated with externally-financed projects, the number of accounts opened under other circumstances has declined. Treasury deposits held by the BCP are still not remunerated (prohibited by law), and the BCP does not charge for its financial services. Treasury deposits in the BCP have grown in recent months to almost US\$700 million in February 2009. This implies a growing opportunity cost, since these resources cannot be invested and are not entirely available for cash management by the Treasury (Source: IMF Report: Strengthening Budget Preparation and Debt Management, February 2009).
- 1.35 The Public Treasury Department (DGTP) of the Ministry of Finance has been conducting an inventory of the central administration's bank accounts at the Central Bank with a view to setting up the Single Treasury Account. This proposed Single Account is designed to allow for the management of virtual accounting accounts separately from specific bank accounts for each entity or type of expenditure, makes it possible to use idle resources (bank accounts the DGTP cannot access), and improves cash management by the Treasury.
- 1.36 In addition, the Ministry of Finance is drafting an amendment to Law 1535 on Financial Management (LAFE), based on the recommendations of the Bank, the IFA 2008, the IMF, and the findings of the Ministry of Finance itself. Specifically, it aims to empower the Treasury to open and close bank accounts in order to implement the CUT, upgrade government accounting, and clarify roles and responsibilities in the National Public Investment System (SNIP), among other things.

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<sup>5</sup> In the World Bank project, the Ministry of Finance is committed to ensuring that in the financial plan for 2009 social spending (including social safety net programs) continue to increase as a proportion of aggregate central government spending in the 2009 budget (in comparison with the previous year's budget). The resources will go mainly on social programs that are proven to be efficient and equitable.

- 1.37 Lastly, the National Public Procurement Division (DNCP) is moving forward with various actions to modernize and improve the efficiency and transparency of the public procurement system, including quality assurance of its processes through ISO 9001:2001 certification and electronic Dutch auctions (SbE). (The first 11 pilot trials carried out in 2009 brought savings of around 20% on initial estimates.)
- 1.38 Other options considered in this area include the adoption of framework agreements for bulk purchases as a mechanism for generating economies of scale and reducing transaction costs for certain products; expansion of the number of mandatory standard specifications for bidding procedures, and other actions to encourage the participation of small- and medium-sized enterprises in public procurements. In this first operation, priority will be given to DNCP certification and expansion of SbE; adoption of the framework agreement will be undertaken in the second operation of this programmatic series.
- 1.39 **Component IV. Public investment system.** General objective: Expand and improve the quality and efficiency of public investment projects, integrating the stages of the project cycle (planning, design, execution, monitoring, evaluation), and promoting improvements in the Ministry of Finance's capacity to analyze and monitor the economic and financial aspects of investment projects carried out in partnership with the private sector. The specific objective of this component in this **first operation** is to design and begin implementing a public investment management model, defining the necessary organizational, methodological, procedural, and technological aspects, and identifying institutional training needs.
- 1.40 In recent years, the area of public investment has been organized into different institutional arrangements, without successfully becoming an effective National Public Investment System (SNIP). Jurisdictional overlaps and lack of clarity between the Ministry of Finance and the Technical Planning Secretariat (STP) are added to the absence of an investment project bank, and insufficient capacity for viability analysis. Moreover, the lack of clarity between the Ministry of Finance and the STP regarding authority to program capital spending, among other problems, hinders the effective execution of budgeted resources, which has resulted in around 40% execution of the investment budget (2004-2006, source IFA 2008). It is felt that an effective SNIP policy could raise execution to at least 60% by 2011-2012, upgrade project viability and quality, and enhance alignment with government priorities.
- 1.41 As in the rest of the region, public investment is low in Paraguay, accounting for 4% of GDP on average. Combined with private investment, total investment in the country is little more than 18% of GDP. The possibility of working with the private sector through innovative models of concessions and public-private partnerships (PPPs) would enable the government to increase total investments in the country. Currently, the Ministry of Public Works and Communications is drafting a proposal to allow airports, roads, and other infrastructure works to be awarded under concessions. In this connection, the Ministry of Finance's capacity to perform economic and financial project analyses needs to be strengthened so these types of

arrangements can be promoted in a fiscally responsible manner and integrated with strictly public investment projects.

- 1.42 **Component V. Central government human resources administration.** General objective: Promote greater efficiency and transparency in central government human resources management. The specific objective of this component in this **first operation** is to help the government design strategies for sizing personnel expenses in the budget preparation process; introduce mechanisms for monitoring personnel management in project executing units (PEUs); and promote improvements in personnel management systems and systems that produce statistics on personnel expenditures.<sup>6</sup>
- 1.43 An important step towards incorporating staff-sizing plans into the budget formulation process of central administration entities is to adopt a strategy to strengthen capacities in the Ministry of Finance and the human resources units of the sectors, as called for under this component.
- 1.44 With regard to the PEUs, the program will support efforts to monitor implementation of Decree 12,255 (May 2008) by conducting an inventory of PEU staffing needs; determining on a quarterly basis how many posts are filled by permanent staff; assessing the quality of the selection procedures adopted; and promoting efforts to reduce staff turnover. The objective of these actions is to improve the PEUs' integration with the ministries and agencies to which they are attached.
- 1.45 The IFA 2008 reports that incomplete records and the absence of a personnel database limit the integrity and effectiveness of personnel roster controls. It also states that it takes considerably longer than three months to introduce changes in the roster, which makes retroactive adjustments a common requirement. While controls do exist, they are inadequate to ensure full data integrity. The program will work through the National Human Resources System (SINARH) to promote greater control of double pay in the roster, and to produce and disseminate personnel statistics.
- 1.46 The policy options selected for this component have to do with the budgetary aspects of personnel and PEU management, aiming to supplement government efforts to revise the civil service's legal framework, with the support of a World Bank programmatic series.

#### **E. Key indicators of the results matrix**

- 1.47 The program's general purpose indicator in the results matrix was **government effectiveness**, prepared by the World Bank Institute, which measures the perception

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<sup>6</sup> Personnel expenditures averaged 7.28% of GDP from 2004 to 2008, and rose from 7.1% in 2007 to 7.5% in 2008. For 2009, while the government requested 7.3% in the proposed budget, Congress approved the equivalent of 8.1%; the IMF estimates that it would be feasible to maintain personnel expenses at around 7.5% of GDP, which would represent a nominal increase of 15% over 2008 (this would require not executing some temporary contracts).

of the quality of public services, the civil service, and policy design and implementation.<sup>7</sup>

- 1.48 For policies related to financial management and public expenditure management, four indicators of Public Expenditure and Financial Accountability (PEFA) of the Integrated Fiduciary Assessment (IFA 2008) were selected: ID-12, which measures the multiyear perspective in fiscal planning, expenditure policy, and budgeting; ID-17, the recording and management of cash balances of the Treasury; ID-19, which measures competition, value for money, and controls in procurement; and ID-18, effectiveness of payroll controls.
- 1.49 Other specific indicators were included: percentage annual execution of budgeted public investments; payments to TEKOPORA beneficiaries through the banking system; average balance in the BCP available for cash management by the Treasury; savings realized from holding electronic Dutch auctions (SbE), among other things.
- 1.50 All indicators, baselines, and impact assessments can be found in Results Matrix (Link 4).

## **II. FINANCING STRUCTURE AND RISKS**

### **A. Financing and contractual conditions**

- 2.1 The total cost of the program is US\$100 million, charged to the resources of the Single Currency Facility of the Ordinary Capital (OC). The special contractual conditions precedent to the single disbursement of the loan are set out in the table in paragraph 4.1.

### **B. Risks and mitigating measures**

- 2.2 The risk analysis conducted during the program preparation stage found this operation to be of moderate overall risk. Three main risks were identified: (a) any significant spreading of the effects of the international financial crisis could undermine macroeconomic stability and impede implementation of the proposed reforms; (b) insufficient political support for the government could hinder or delay approval of this operation in Congress, and of the two legislative bills referred to in the conditions for disbursement; and (c) the Ministry of Finance may not have the human, technological, and financial resources to implement and sustain the reforms.
- 2.3 The Ministry of Finance has been taking measures to mitigate these risks, which are being monitored on an ongoing basis by the project team. With regard to maintaining macroeconomic stability, the new government that took office in August 2008 is continuing to implement a responsible fiscal and monetary policy, with persistent purpose and ongoing monitoring. Concerning the

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<sup>7</sup> There are no general, regularly produced indicators that can be used to effectively measure this program's purpose; government effectiveness was chosen because it is closest to what needs to be measured. Nonetheless, it is based on rankings, which should be borne in mind in assessing overall program impact.

political support needed to secure the approval of this loan by Congress, and approval of the two legislative bills, the Ministry of Finance plans to submit an integrated set of initiatives making up the Economic Reactivation Plan to mitigate the effects of the international financial crisis on the country, which boosts the possibility of obtaining program approval. If the two legislative bills are not approved, a portion of the reforms will be implemented through the issuance of other decrees envisaged in the program. Finally, to strengthen the Ministry of Finance's capacity for implementing and sustaining the reforms, resources from PROFOMAF II and other existing Bank-financed operations (see paragraph 1.18) are available to support the Ministry of Finance.

- 2.4 **Environmental and social risks.** No environmental and social risks are associated with the present program since it involves only institutional strengthening activities. In accordance with Directive B-13, and taking into account the findings of the Safeguards Policy Filter Report, this operation does not require classification.

### III. IMPLEMENTATION AND MANAGEMENT PLAN

#### A. Summary of agreements reached for implementation

- 3.1 The borrower will be the Republic of Paraguay and the executing agency the Ministry of Finance, which will hold primary responsibility with respect to the Bank, work with it directly, and define the program's course of action. Virtually all decisions and technical actions required for implementing the program fall within the sphere of action or authority of the Ministry of Finance which, through each relevant entity, will be responsible for adopting the decisions agreed upon and implementing the specific actions.
- 3.2 **Disbursements and execution.** The term for the single disbursement of the operation is 24 months.

#### B. Summary of agreements reached for monitoring performance

- 3.3 **Monitoring and evaluation.** The targets and indicators of progress and success agreed to with the Ministry of Finance, set out in the results matrix (Link 4), will be taken into account for the purposes of program monitoring and evaluation. Project performance monitoring reports (PPMR) will be completed annually, one for each operation, and one project completion report (PCR) will be prepared at the conclusion of the programmatic series.
- 3.4 **Policy letter.** The Bank reached agreement with the Government of Paraguay on the macroeconomic and sector policies contained in the policy letter sent by the Ministry of Finance to the Bank (Link 2).

### IV. MATRIX OF CONDITIONS FOR DISBURSEMENT

- 4.1 The policy matrix (Annex II) contains all the reform objectives and actions expected for the 2009-2010 period. The commitments of this first operation of the



programmatic series related to this loan are set out below in the **Matrix of Disbursement Conditions**.

Disbursement condition	Means of verification
1. <u>Macroeconomic stability</u>	
1.1 Maintain a stable macroeconomic policy framework consistent with program objectives and the guidelines set out in the <b>sector policy letter</b>	1.1 Macroeconomic assessment report prepared by the Bank
2. <u>Public policy coordination and efficiency</u>	
2.1 <b>Organizational reform of the economic area</b> of the Executive Branch designed; includes increased integration of planning and execution functions in public spending	2.1 <b>Legislative bill to amend Law 109</b> (of 1992) <b>submitted to Congress</b>
2.2 <b>Proposed reorganization of the social area</b> designed; includes increased sector integration and coordination	2.2 <b>Executive Branch decree enacted, calling for realignment</b> of the social area and reorganization of its structures
2.3 Control procedures and systems for <b>cash transfers with shared responsibility</b> reviewed, including creation of the <b>single list</b> of TEKOPORA beneficiaries, and a plan for making <b>payments through the banking system</b>	2.3 <b>Action plan</b> on procedures for <b>TEKOPORA</b> cash transfers, including monitoring and outcomes indicators, and a plan for making payments through the banking system, <b>approved by the Minister of Finance</b>
3. <u>Public expenditure management systems</u>	
3.1 Coverage of the <b>Single Treasury Account (CUT)</b> expanded with actions to increase the amount of resources in the Central Bank available for cash management by the Treasury	3.1 <b>Executive Branch decree</b> enacted establishing strategy and scope of the CUT, and ordering an <b>inventory and indicators</b> of Treasury accounts
3.2 Bill to amend the <b>Law on Financial Administration - LAFE (N°1535/1999)</b> submitted to Congress	3.2 <b>LAFE bill submitted to Congress</b> authorizes the Treasury to implement the CUT, make improvements in accounting, and clarify roles and responsibilities in the National Public Investment System (SNIP)
3.3 Modernization of the <b>public procurement system</b> expanded by improving efficiency and obtaining certification of the quality of its processes	3.3 Thirty pilot <b>electronic Dutch auctions (SbE)</b> held; DNCP receives <b>ISO 9001:2001</b> certification
4. <u>Public investment system</u>	
4.1 Establishment of a National Public Investment System (SNIP) under way, with institutional roles and responsibilities defined in the <b>public investment</b> programming process	4.1 <b>Executive Branch decree enacted establishing the SNIP</b> , consistent with the proposal for organizational reform of the economic area and the proposal to amend the LAFE
4.2 <b>Budget programming</b> of public investment projects strengthened and integrated by linking the <b>Operations Programming System (SPO)</b> with the <b>Integrated Financial Management System (SIAF)</b> , being implemented	4.2 Bank <b>verification</b> of the systems confirms that SPO has been integrated into the SIAF, at the level of a pilot experience
4.3 Ministry of Finance <b>plan</b> for analyzing and monitoring economic and financial aspects of <b>concessions and public-private partnership investments (PPPs)</b> , approved	4.3 <b>Decision</b> as to which Ministry of Finance unit will be responsible for the economic and financial aspects of concessions and PPPs; <b>plan</b> to strengthen the Ministry's capacity for viability analysis, risk management, and for monitoring guarantees and liabilities related to

Disbursement condition	Means of verification
	concessions and PPPs, approved by the Minister of Finance and published on the Ministry's web site
5. <u>Central government human resources administration</u>	
<p>5.1 <b>Guidelines of a strategy for budgetary administration of human resources</b> approved; includes proposals for strengthening staff-sizing capacity in the budget preparation process</p> <p>5.2 Plan formulated to <b>monitor implementation of Decree 12,255</b> (May 2008); includes a mechanism for monitoring how many posts in program executing units (PEUs) are filled by permanent staff members.</p> <p>5.3 Promote improvements in personnel expenditure policies and management systems; includes use of <b>the SINARH to produce statistics and analyze personnel expenditures</b></p>	<p>5.1 <b>Guidelines</b> of the strategy for budgetary administration of human resources approved by the Minister of Finance</p> <p>5.2 <b>Plan to monitor Decree 12,255</b> approved by the Minister of Finance, including an inventory of staffing needs of PEUs; quarterly determination of number of posts filled by permanent staff; analysis of the quality of selection procedures, and an indicator of staff turnover.</p> <p>5.3 <b>Evaluation</b> approved by the Minister of Finance in coordination with the STP and posted on the Ministry's website; includes analysis of personnel expenditures and of the application of Decree 223 (September 2008) on the control of double pay.</p>

## PUBLIC MANAGEMENT MODERNIZATION PROGRAM

(PR-L1043)

### POLICY MATRIX

Policy components	Commitments for the first operation (US\$100 million - 2009)	Estimated commitments for the second operation (US\$50 million - 2010)
<b>1. Macroeconomic stability</b>	<u>End objective:</u> Macroeconomic stability	
	Maintain a stable macroeconomic policy framework consistent with program objectives and the guidelines set out in the <b>sector policy letter</b> .  <u>Proof:</u> <b>Macroeconomic Evaluation Report</b> prepared by the Bank.	Maintain a stable macroeconomic policy framework consistent with program objectives and the guidelines set out in a <b>sector policy letter</b> .  <u>Proof:</u> <b>Macroeconomic Evaluation Report</b> prepared by the Bank.
<b>2. Public policy coordination and efficiency</b>	<u>End objective:</u> Reduce organizational overlaps and promote greater coordination and efficiency in public policy formulation, execution, and evaluation in the main public spending categories, with special emphasis on the economic and social sectors	
	2.1 <b>Organizational reform of the economic area</b> of the Executive Branch designed; includes greater integration of planning and execution functions in public spending  <u>Proof:</u> <b>Bill to amend Law 109</b> (of 1992) <b>submitted to Congress</b>	2.1 Organizational reform of the economic area <b>in progress</b>  <u>Proof:</u> Bill submitted by Ministry of Finance to amend Law 109 (of 1992) examined by Congress and other implementing actions confirmed
	2.2 Proposal for <b>organizational realignment of the social sector</b> prepared; includes greater sector integration and coordination  <u>Proof:</u> <b>Executive Branch decree ordering realignment</b> of the social sector and reorganization of its structures enacted.	2.2 Reorganization of the social sector <b>in progress</b>  <u>Proof:</u> Regulatory framework updated and other implementing actions confirmed
	2.3 Control procedures and systems for <b>cash transfers with shared responsibility</b> reviewed; includes establishment of the <b>single list</b> of TEKOPORA beneficiaries and a plan to <b>make payments through the banking system</b> .  <u>Proof:</u> <b>Action plan</b> for procedures for <b>TEKOPORA</b> cash transfers; includes monitoring and outcomes indicators, and plan to make the payments through the banking system, <b>approved by the Minister of Finance</b>	2.3 <b>Evaluation</b> designed for <b>TEKOPORA</b> control procedures and systems  <u>Proof:</u> Process evaluation report approved and published, including an analysis of the list of beneficiaries and the arrangement for making payments through the banking system

Policy components	Commitments for the first operation (US\$100 million - 2009)	Estimated commitments for the second operation (US\$50 million - 2010)
<b>3. Public expenditure management systems</b>	<p><u>End objective:</u> Promote greater integration, quality, and transparency of information from the cross-cutting systems that support public expenditure management, including treasury, accounting, budget, and public procurement.</p>	
	<p>3.1 Coverage of the <b>Single Treasury Account (CUT)</b> expanded, including actions to increase the amount of resources in the Central Bank available for cash management by the Treasury</p> <p><u>Proof:</u> <b>Executive Branch decree</b> enacted establishing the strategy and scope of the CUT, and that orders an <b>inventory and indicators</b> of Treasury accounts</p>	<p>3.1 <b>SIAF Treasury module</b> operates with the expanded management of the Single Account, in line with the Decree on CUT</p> <p><u>Proof:</u> Bank verification of SIAF alignment with the decree</p>
	<p>3.2 Bill to amend the <b>Financial Management Act (LAFE) (1535/1999)</b> submitted to Congress</p> <p><u>Proof:</u> <b>LAFE bill submitted to Congress;</b> includes empowering the Treasury to implement the CUT, to make improvements in accounting, and to clarify roles and responsibilities in the National Public Investment System (SNIP)</p>	<p>3.2 Financial Management Act in force</p> <p><u>Proof:</u> Bill <b>reviewed by Congress</b></p>
	<p>3.3 Process to modernize the <b>public procurement system</b> expanded, with improvements in efficiency and process quality certification</p> <p><u>Proof:</u> 30 pilot <b>electronic Dutch auctions (SbE)</b> conducted; DNCP receives <b>ISO 9001:2001</b> certification.</p>	<p>3.3 Process to modernize the <b>public procurement system</b> deepened, including expansion of SbE and introduction of framework agreements</p> <p><u>Proof:</u> <b>SbE system expanded to cover 15%</b> of central administration procurements; and <b>pilot framework agreement</b> prepared</p>
<b>4. Public investment system</b>	<p><u>End objective:</u> Expand and improve the quality and efficiency of public investment projects, integrating the stages of the project cycle (planning, design, execution, monitoring, and evaluation), and promoting improvements in the Ministry of Finance's capacity to analyze and monitor the economic and financial aspects of investment projects carried out in partnership with the private sector.</p>	
	<p>4.1 Establishment of a National Public Investment System (SNIP) with institutional roles and responsibilities established in the <b>public investment</b> programming process.</p> <p><u>Proof:</u> <b>Executive Branch decree</b> enacted establishing the <b>SNIP</b>, consistent with the proposal for organizational reform of the economic area and the legislative bill to amend the LAFE</p>	<p>4.1 SNIP in operation</p> <p><u>Proof:</u> Unit responsible for SNIP established and staff received training in viability analysis methodologies; project bank created</p>

Policy components	Commitments for the first operation (US\$100 million - 2009)	Estimated commitments for the second operation (US\$50 million - 2010)
	<p>4.2 <b>Budget programming</b> of public investment projects strengthened and integrated by creating a link between the <b>SPO</b> (Operations Programming System) <b>and the SIAF</b> (Integrated Financial Management System), in implementation</p> <p><u>Proof</u>: Bank verification of the systems determines that SPO has been integrated into the SIAF at the pilot level.</p>	<p>4.2 SPO is linked to the SIAF</p> <p><u>Proof</u>: Bank's <b>verification of the systems</b></p>
	<p>4.3 Ministry of Finance <b>plan</b> for analyzing and monitoring the economic and financial aspects of <b>concessions and public-private investment partnerships</b> (PPPs) approved</p> <p><u>Proof</u>: Identification of the Ministry of Finance unit responsible for the economic and financial aspects of concessions and PPPs, and plan to strengthen the Ministry's capacity for viability analysis, risk management, and monitoring of guarantees and liabilities generated by concessions and PPPs, approved by the Minister of Finance and published on the ministry's website</p>	<p>4.3 Ministry of Finance plan for analyzing and monitoring the economic and financial aspects of <b>concessions and PPPs</b>, in implementation</p> <p><u>Proof</u>: Ministry of Finance unit responsible for economic and financial aspects of concessions and PPPs received training and is functioning</p>
<b>5. Central government human resources administration</b>	<p><u>Final objective</u>: Promote greater efficiency and transparency in central government personnel management</p>	
	<p>5.1 <b>Guidelines of a strategy for budgetary administration of human resources</b> approved, including proposals for strengthening staff-sizing capacity in the budget preparation process</p> <p><u>Proof</u>: Guidelines of a strategy for budgetary administration of human resources approved by the Minister of Finance</p>	<p>5.1 <b>Staff-sizing plans</b> incorporated into the budget formulation process of the central administration</p> <p><u>Proof</u>: Decree on budgetary guidelines instructs entities of the central administration to present their strategic plans and staff-sizing plans as part of the 2011 budget preparation process</p>
	<p>5.2 <b>Plan to monitor implementation of Decree 12,255</b> (May 2008) established; includes a mechanism for monitoring how many program executing unit (PEU) positions are filled by permanent staff members</p> <p><u>Proof</u>: <b>Plan to monitor Decree 12,255</b> approved by the Minister of Finance; includes an inventory of PEU staffing needs; quarterly determination of positions filled by permanent staff; analysis of the quality of selection procedures adopted, and staff turnover indicator</p>	<p>5.2 Program executing units are professionalized</p> <p><u>Proof</u>: Report determines that at least 50% of professionals are retained as permanent staff members in the PEUs; indicators are added for the number of staff, the quality of selection procedures, and staff turnover</p>

Policy components	Commitments for the first operation (US\$100 million - 2009)	Estimated commitments for the second operation (US\$50 million - 2010)
	<p>5.3 Promote improvements in personnel expenditure policies and management systems, including use of <b>SINARH for producing statistics and analyzing personnel expenditures</b></p> <p><u>Proof:</u> <b>Evaluation</b> approved by the Minister of Finance in coordination with the SFP and posted on the ministry's website; includes an analysis of personnel expenditures and application of Decree 223 of September 2008 on the control of double pay.</p>	<p>5.3 SINARH makes all <b>payments</b> for central Executive Branch remuneration through the <b>banking network, and the Ministry of Finance continues to produce statistics and analyze personnel expenditures</b></p> <p><u>Proof:</u> Bank verification of the system, and posting on the ministry's website of statistics and personnel expenditure analysis</p>