STRENGTHENING OF LOCAL GOVERNMENT ADMINISTRATIONS

(CO-0155)

EXECUTIVE SUMMARY

BORROWER:	Financiera de Desarrollo Territorial S.A. (FINDETER).	
GUARANTOR:	Republic of Colombia.	
EXECUTING AGENCY:	FINDETER and the Ministry of Finance and Public Credit.	
AMOUNT AND SOURCE:	IDB:	US$40.0 million (OC)
	CAF cofinancing:	US$25.0 million
	Local counterpart funding:	US$ 7.5 million
	Total:	US$72.5 million
FINANCIAL TERMS AND CONDITIONS:	Amortization period:	20 years
	Disbursement period:	42 months
	Interest rate:	variable
	Inspection and supervision:	1%
	Credit fee:	0.75%
	Currency:	United States dollars from the Single-Currency Facility.
COFINANCING:	Andean Development Corporation (CAF)	
	Amortization period:	8 years
	Disbursement period:	2 years
	Interest rate:	variable
	Inspection and supervision:	1%
	Credit fee:	0.75%

OBJECTIVES:

The overall objective of the program is to help consolidate the decentralization process in Colombia which requires: (i) ensuring that departmental and local governments are fiscally sound; and (ii) strengthening the capacity of the central government to manage the tax system and correct the fiscal imbalances of local administrations.

Ensuring fiscal viability at the local level will require introducing economic reforms in the departmental and local governments (DLGs), including measures designed to bring their finances back into balance. The present program will reinforce this effort by providing institutional strengthening for

DLGs aimed at modernizing their tax administrations and making certain that the reforms are sustainable.

At the same time, the program seeks to improve the central government's capacity to manage intergovernmental fiscal relations. Hence, the program will bolster the relevant institutions at the central level and improve the information available on regional indebtedness by creating a Registry of Debt and Guarantees (REG).

DESCRIPTION:

The Ministry of Finance and Public Credit (MFPC) will head the program and provide the means for bringing about structural change in the DLGs. The multilateral agencies will make disbursements to FINDETER as an advance of funds, and the latter will create a fund to finance the programs for modernization and reform of local governments.

Before receiving resources from the fund, the DLGs must submit a Local Government Economic Reform Plan (PRET) to a Loan Committee (CC) for approval. The DLGs benefitting from the program must provide assurances that they will carry out the economic reforms within their jurisdictions. With this in mind, they will be required to set specific fiscal performance goals and take the necessary steps to meet these targets. Funds will be disbursed to the DLGs in tranches when the goals have been reached and upon completion of the specified activities. Resources from the fund are expected to finance activities in approximately 10 DLGs.

These resources will be allocated through the financial intermediaries (FIs) which will rediscount the loans with FINDETER and assume between 50% and 80% of the overall risk. The remaining risk will be covered by the central government through a trust created for this purpose.

Evaluation and monitoring of compliance with the performance agreements will be the responsibility of the Central Technical Unit (UTC), which will report to the CC and be made up of members of the Ministry of Finance's Fiscal Support Directorate (DAF) and FINDETER.

The resources will be used by departmental and local governments to fund: (i) administrative reforms; (ii) transfer of assets (privatization, granting of concessions, etc.); and (iii) technical assistance in tax administration, financial administration and management of human resources.

At the central level, the resources will be used to finance: (i) the institutional strengthening for the DAF, which will help the UTC to evaluate and supervise the program; and (ii) the creation of the REG, which is necessary to improve the quality of data on taxes levied by the DLGs.

ENVIRONMENTAL CLASSIFICATION: At its meeting of May 7, 1996, the Environment Committee classified this as a Category II operation.

APPROVAL PROCEDURE: In accordance with the rules adopted by the Board of Executive Directors (Document DR-398-2), this proposal must be placed before the Committee of the Whole for approval inasmuch as it contains innovative features.

BENEFITS: Carrying through on government decentralization is one of the objectives laid down in Colombia's constitution, and its achievement will have a positive impact both on the country's ability to provide social services, and on the willingness of the public to participate in the decision-making process.

The proposed program will aid in the consolidation of the decentralization process. Specifically, it is designed to strengthen departmental and local governments by means of institutional modernization and reform so that they can balance their budgets. Since most of the country's spending on social sectors is allocated by the DLGs, the program is also expected to result in greater efficiency in the delivery of social services. As well, the institutional strengthening of the DLGs' will help raise the profile of the State in areas where, traditionally, there has been little respect for the exercise of public authority.

Moreover, the program will not only strengthen the technical capacity of the DAF, but will also upgrade and improve the leadership capacity of other institutions in the central government. This leadership by the central government will be accompanied by a systematic attack on fiscal deficits at the local level, which will give greater transparency and credibility to both the institutions themselves and the mechanism employed.

Creation of the REG will likewise help to generate timely and reliable data on taxes levied by the regional administrations. This will have a positive effect both on fiscal administration at the central

and local levels alike, and on the effort to ensure transparency in the granting of loans by the FIs.

Accordingly, under this program a mechanism will be created enabling governments to respond systematically to the need for reform of public finances and strengthening of the institutions responsible for tax management at the regional level.

SPECIAL CHARACTERISTICS OF THE OPERATION: Given the importance placed on administrative restructuring in the reforms being introduced in the DLGs, one of the main items of expenditure under the program will be the separation package for personnel displaced by the process and whose positions are eliminated. This item will account for nearly 60% of the total cost of the program, but is considered essential for pressing ahead with the modernization of government at the subnational level.

This activity will be supplemented with strengthening for institutions in the public sector that are responsible for fiscal management, pursuant to the mandate of the Eighth Replenishment of Resources concerning modernization of the State and deepening of the process of decentralization.

RISKS: The main risk in this operation has to do with the sustainability of the reforms. The success of these initiatives is directly dependent on the political support that they receive from governors, mayors and their respective legislative bodies. A change in political leadership at the district and municipal level could signify a possible reversal of the reforms.

The assessment and oversight duties of the UTC to be created under this program is therefore vital. And to further mitigate this risk, program funds will be disbursed in tranches to remove any possibility of improper use of resources.

Another risk stems from the participation of FIs in the program, and the chance that some beneficiaries may turn out to be poor credit risks. To counter this risk, the government will establish a trust covering a variable percentage of each transaction, ranging from 20% to 50% of the amount of individual loans. In addition, the Loan Committee (CC) will be empowered to change the lending spreads in the event that these prove inadequate for ensuring participation by the FIs.

THE BANK'S COUNTRY AND SECTOR STRATEGY:

In August 1995, the Board of Executive Directors of the IDB approved the country programming paper for Colombia (GN-1886) setting out the Bank's strategy for that country during the 1995-1997 period.

The strategy adopted is based on a study of the principal challenges that the country will face over the next few years, and involves a three-pronged attack: (i) supporting direct investment in the social sectors as a means of alleviating poverty and raising the standard of living of the population; (ii) strengthening the management of public institutions in order to make public expenditures more efficient; and (iii) encouraging greater private sector participation through a series of initiatives aimed at increasing economic productivity. The proposed operation is specifically identified in the CPP.

PROCUREMENT THRESHOLDS:

Procurement will be done by international competitive bidding for contracts valued at US$350,000 or more in the case of goods and related services and US$200,000 or more in the case of consulting services.

SPECIAL CONTRACTUAL CONDITIONS:

As a condition precedent to the first disbursement of the loan, the borrower must submit:

1. Evidence that the REG has been duly created (see paragraph 3.19).
2. Proof that the Credit Regulations and model contracts required for the program have been approved (see paragraph 2.20).
3. Tentative schedules for: (i) processing the PRETs; and (ii) disbursements to local government administrations (see paragraph 3.34).
4. Proof that the Operating Regulations for the trust fund have been drafted and approved (see paragraph 3.14).
5. Evidence that the UTC had been set up and the corresponding personnel designated (see paragraph 3.5).

Additional contractual conditions are described in the following paragraphs: 3.35 (advance of funds of up to 20%), and 3.43 (final evaluation).

IMPACT ON POVERTY:

Not applicable.

I. FRAME OF REFERENCE

A. Recent economic context

1.1 The Colombian economy is experiencing some difficulty at the moment and growth is expected to slow to 3.5% in 1996, which is below its average for the last three years although still above the average rate of growth for Latin America as a whole. The damaging effects of the political crisis have combined with aspects of the current economic cycle to slow economic expansion.

1.2 The country's fiscal policy has been expansionary in recent years as a result of both conscious political decisions (greater spending on social sectors) and legislative action (new mandates for the decentralization process and social security reform). Monetary policy has been tightened to reduce the rate of inflation, but the results have not been altogether satisfactory as reining in inflation has proven more difficult than expected. Restricting the money supply has pushed interest rates to nearly 20% in real terms, while inflation has stubbornly remained at 19%.

1.3 The main challenge in macroeconomic terms is to reduce the central government deficit which will equal 3.5% of GDP in 1996 and is showing signs of increasing further. A significant proportion of the federal outlays is in non-discretionary spending, which means that it will be necessary to build a political consensus and amend the nation's laws to keep the deficit from growing.

1.4 By law, transfers to departmental and local governments (DLGs) and to the social security system must increase annually, whereas these same sectors do not generate the savings required to offset the central government deficit. Also, the finances of some DLGs have slipped badly even though the overall deficit for local administrations amounted to less than 0.8% of GDP in 1995.

1.5 Faced with its fiscal complexities, the government has proposed a series of measures aimed at keeping the central administration's deficit. The Social and Economic Policy Council of Colombia (CONPES) outlined these measures in Official Document No. 2863 of July 1996, noting that unless corrective action is taken the national deficit will continue to widen, producing unstable macroeconomic conditions. Included among these measures are the sale of public enterprises, downsizing of the State, cutting back on transfers to municipalities and the social security system, and keeping increases in public sector wages below the rate of inflation. It is entirely possible that some of these proposals will fail to receive the required consensus for their approval.

B. The decentralization process

1. Rationale, legislation and institutional framework

1.6 The constitutional reform of 1991 had as its goal to strengthen conditions of governance in Colombia, in pursuit of which it redoubled the process of political and administrative decentralization. While the new Constitution may not have established a new model for decentralization, it did succeed in reorganizing and accelerating the process.

1.7 This required giving citizens a greater role in political decision-making at the local level since both responsibility for basic social services and the resources necessary for their delivery were being transferred to the DLGs. The legal basis for this change was enacted in Law 60 of 1993, along with other legislation in each sector.

1.8 Despite the achievements to date, the decentralization process still faces enormous challenges. Accordingly, CONPES Document No. 2788 points to the need to: (i) establish effective coordination of the process; (ii) allocate responsibilities among the different levels of government; and (iii) make DLGs financially sound and strengthen their institutions.

1.9 The document establishes the Ministry of the Interior as the ministry responsible for coordinating the decentralization process, and assigns to the Ministry of Finance and Public Credit (MFPC) the task of reviewing the powers of regional governments with respect to taxation and borrowing, and developing a program of reforms to overhaul their financial and fiscal performance. Finally, CONPES asks MFPC to work together with the National Planning Department (DNP) in reviewing the system of transfer payments.

2. Intergovernment fiscal relationships

1.10 As in most of the countries in the region, fiscal relations between different levels of government in Colombia suffer from a number of difficulties, explained in part by: (i) complicated distribution of powers of taxation at the subnational level; (ii) systems of transfer payments that have yet to incorporate modern practices; and (iii) problems with rules for borrowing by local administrations. In many cases, this situation has been exacerbated by institutional weaknesses preventing the DLGs from making efficient use of the resources they receive.

a. Fiscal revenue

1.11 Colombia has been undertaking gradual fiscal reforms since the 1980s, yet the measurable progress achieved with the central government's tax system has been slow in reaching other levels of administration. Although the departments administer 12 different

taxes, 85% of their tax receipts come from excise levies on beer, alcohol and cigarettes. And this situation is repeated at the municipal level in both the number of taxes collected (16) and the degree of reliance on property tax, business taxes, and vehicle and road taxes.

1.12 Despite administering a large number of taxes, the DLGs have little in the way of taxation infrastructure since the basis of assessment, tax rates, and (in many cases) the distribution of revenues are dictated by federal legislation. Thus, the most important task left to local governments is simply that of collecting the tax revenues themselves.

1.13 Legislation is currently being drafted to overcome the main problems confronting subnational taxation in Colombia. This bill calls for simplification of the system including elimination of certain taxes and consolidation of others levied on similar economic transactions, which are actually administered by the departments and the municipalities.

b. Regional transfers

1.14 Law 60 established the DLGs responsibility of the DLGs in the delivery of basic social service. In essence, the departments were given responsibility for current expenses related to these services, while municipalities are responsible for investment in social infrastructure. 1/

1.15 Transfers from the central government are allocated: (i) in the form of subsidy payments to departments and districts; and (ii) through municipal participation in the case of districts and municipalities. The amount of these transfers is calculated as a share of the central government's current revenues. In 1996, subsidies to departments and districts will account for 24.5% of current revenues, while transfers to municipalities will take another 17%.

1.16 The system of regional transfers suffers from a number of problems which include: (i) earmarking of funds, which removes any incentive for using resources more efficiently; (ii) rigidity of expenditures which are tied to current revenues; and (iii) little incentive to raise resources locally (fiscal inertia).

1/ Under Colombian legislation, the national government must certify the capacity of DLGs to administer the fiscal resources under their jurisdiction. By mid-1996, only 9 departments and 3 districts had received certification in the field of education; while 11 departments, 4 districts and 21 municipalities had been certified in the health sector.

1.17 The Colombian Congress was supposed to review Law 60 in 1996, although the matter has now been put off until 1997. Debate centers on a report prepared by the Commission for Restructuring of Public Finance and Expenditures, which proposes: (i) to consolidate transfers and link them to growth in the GDP; (ii) to tie transfer payments for health and education to the cost of providing these services; and (iii) to establish freely distributable transfer payments.

c. Borrowing

1.18 Internal borrowing by local governments rose from 1% of GDP in 1993, to almost 3% in 1995, as a result of the greater share of resources and responsibilities alike that were assigned to local administrations beginning in 1991. The granting of greater regional autonomy added considerably to spending (particularly the current expenditures) of some administrations, while the increase in the volume of resources handled by the departments and municipalities made them potentially attractive clients for the nation's financial system.

1.19 Domestic borrowing by the DLGs is regulated in terms of demand and by the supply of credit. In the area of demand, current legislation links borrowing by DLGs to revenue, which has the disadvantage of ignoring the debt-servicing capacity of borrowers. The effort to control regional borrowing by regulating demand for credit has met with only moderate success, largely because of the central government's inability to enforce the legislation.

1.20 Beginning in 1995, the Office of Banking Supervision (SB) tightened limits on the supply of regional credit to as a way of reducing the risk to the nation's financial system of loan losses due to insolvency problems among the DLGs. These regulations were effective in that they discouraged lending to DLGs that were undergoing financial difficulties. Yet despite this strengthening of control by the SB, lack of information on borrowing by DLGs remains a serious problem.

1.21 Two points must be noted in connection with the recent growth in DLG borrowing. First, that the significant increase in debt load has not caused a macroeconomic crisis is due to the initially low level of indebtedness. Second, there is no correlation for DLGs between high levels of debt in absolute terms, and financial difficulties in servicing these obligations. 2/

2/ It is estimated that five departments account for around 50% — and the top 10 account for 72% — of departmental indebtedness, while the municipalities of Medellín, Cali, Bogotá and Barranquilla together represent nearly 45% of total municipal debt.

1.22 A bill is currently before Congress that would regulate local government debt. This legislation will limit the borrowing of DLGs based on their debt-servicing capacity as measured by an indicator of creditworthiness: namely, the ratio of interest payments on the debt to operational savings (current revenues less current expenditures, excluding interest).

C. The finances of local governments

1. Fiscal performance

1.23 The fiscal performance of the DLGs shows considerable variation. For example, the fiscal indicators for Atlántico, Valle and the municipality of Medellín are relatively sound, whereas the situation in La Guajira, Chocó and the municipality of Montería show signs of real difficulty. 3/

1.24 It is possible to identify certain general factors which are common to DLGs that are experiencing financial difficulties: (i) a recent decline in tax receipts; (ii) rising costs due to overstaffing, substantial transfers to decentralized agencies, and excessive pension liabilities; and (iii) uncontrolled growth in public debt. These problems are compounded by shortcoming in budgetary institutions at all levels responsible for fiscal management at the subnational level.

1.25 On the revenue side, as a result of an increase in smuggling, tax proceeds fell in real terms for local governments. In addition, there are indications that the increased transfers may have induced fiscal laxity in the regions. When the weakness of local tax collection systems is added, unsurprisingly, taxes accounted for less than 30% of total revenues in a third of all departments and municipal capitals in 1995.

1.26 At the same time, many local governments have seen a noticeable increase in expenditures as a result of ill-advised policies which have led to a sharp rise in staffing levels, in both central administrations and decentralized agencies. Operating expenses now account for over 95% of current revenues in a quarter of Colombia's departments, and in close to one half its municipal capitals.

1.27 In 1995, a total of 19 departments and about one half the municipal capitals reported a fiscal deficit. Since most of the underlying causes for this are structural in nature, these governments have

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3/ Evaluating the fiscal performance of the DLGs is made difficult by the lack of reliable data. Various sources of information (MHyCP, DNP, Comptroller General's Office, local governments) give results that are not always consistent. The conclusions given in this section are based on data generated by the Comptroller General's Office (CGR) and the General Accounting Office (DGCP) for 1995.

been operating at a deficit in past years as well. During those years, the shortfall was covered by bank loans guaranteed by future revenues, resulting in heavy and rapidly growing interest payments. Because of their critical financial condition, some of these administrations have only restricted access to further credit, and are expected to default on their obligations shortly.

1.28 Excessive debt levels are threatening the financial solvency and sustainability of some local governments. Taking as an indicator the debt-service-to-current-revenues ratio, it can be seen that 9 departments, 3 districts and almost 15% of municipal capitals have already exceeded the legal limit of 30%. Moreover, interest payments now exceed 40% of operational savings in 7 departments and in one-fifth of municipal capitals — a sure sign that these entities will have difficulty servicing their debts in future. Lastly, the sustainability of the debt load is a problem for six departments, two districts and close to 10% of municipal capitals in Colombia, for which total debt now exceeds 80% of current revenues.

2. The 1995-1996 performance pacts

1.29 In 1995-1996, the national government began responding to the insolvency problems of the DLGs by granting loans to the departments of Chocó, Nariño, Putumayo and La Guajira, to be disbursed on condition that they introduce reforms and attain specific fiscal targets. 4/ Each of these loans was in the amount of US$5 million, to be drawn on the national treasury. The performance pacts themselves were designed and monitored by the Fiscal Support Directorate (DAF), which is a division of the MFPC.

1.30 In these pacts, the departments committed themselves, among other things, to: (i) trim current expenditures by reducing staff, renegotiating contracts for services and refinancing their debt with the commercial banks; (ii) place limits on fixed capital investment; (iii) restructure their business activities; and (iv) increase fiscal revenues.

3. Lessons learned from the 1995-1996 performance pacts

1.31 Although they are still in progress, the experience gained in the first three pacts mentioned above were analyzed during preparation of the present program. 5/ Table 1 summarizes the results of an evaluation of compliance with the principal provisions of the agreements.

4/ A forerunner of these operations was a 1993 loan to the department of Chocó, although no further details are available.

5/ The performance pact with the department of La Guajira was only signed in May 1996, so that no information on its outcome was available during preparation of the present program.

Table 1

1995 performance pacts

Provisions	Chocó	Nariño	Putumayo
Write-off of delinquent accounts	C	N/A	N/A
Refinancing commercial debt	C	C	C
Increased fiscal revenues	C	N/D	C
Trim staff	P	P	C
Freeze per diems for Members of Legislature	N	N	N
Reduce payments for services	N	N/D	N/D
Reduce transfers to government enterprises	N/A	N/D	P

Notes: C means that the department complied with the pact;
P indicates partial compliance;
N indicates no compliance;
N/A = not applicable;
N/D = no data.

1.32 Among the factors favoring due compliance with the pacts are the following: (i) the political commitment of the governors; (ii) the technical assistance provided by the DAF which has had a great impact despite being limited by lack of resources; and (iii) the immediate availability of financial resources to pay for staff reductions and associated severance payments, thereby reducing the political costs of such measures.

1.33 Nevertheless, some of the provisions in these pacts have been difficult to meet. Among the problems worth noting are: (i) the political difficulty involved in carrying out massive layoffs in departments which suffer from poverty, unemployment and civil unrest; (ii) the fact that competing in the new context requires meeting a certain minimum level of expenditures beyond which it is difficult to make any further reductions; (iii) the lack of commitment on the part of departmental legislatures; and (iv) outmoded administrative systems in by the DLGs.

1.34 The main lesson that can be drawn from recent efforts to put their fiscal houses in order and that can be applied by DLGs in future programs is the need to strengthen the capacity of the central government to carry out its measures and ensure that these are consistent with the commitment to economic reform across the country.

1.35 Among the most important recommendations are that any future program must be designed to: (i) ensure that all DLGs are treated equally by organizing the activities in systematic fashion; (ii) propose effective means for repayment of loans;

(iii) reinforce the capacity of the central government to supervise programs; (iv) enhance the capacity of beneficiary entities to execute programs; (v) help ensure that economic reforms are sustainable by providing a complete range of institutional strengthening activities in the fiscal area; (vi) improve the information available to DLGs; and (vii) elicit a commitment from the local legislatures.

4. Institutional and technical development

1.36 The DLGs are autonomous bodies with their own organization and financial management. The agency responsible for administering resources in each case is the Finance Secretariat which provides basic revenue, budget and accounting services, and performs treasurer's duties. Public debt is generally handled by the Office of the Secretary of Finance.

1.37 Only a small percentage of staff have professional qualifications in each area, and the distribution of personnel is inadequate. The number of different job classifications has proliferated, frequently with only one official per classification. Moreover, pay often differs for positions at similar levels and there is no system for promoting personnel or adjusting wages. In some cases the number of former employees drawing pensions is greater than those on the active payroll.

1.38 Because of a lack of management capacity, some DLGs have little in the way of available data. Despite a legal duty to maintain up-to-date information systems, many local governments lack such systems and have no reliable basic figures on fiscal management in their area. This lack of data is exacerbated by the information demands from various public sector bodies.

1.39 To remedy this situation, the DLGs were directed to forward information to the General Accounting Office (DGCP) in the format specified for the Standard Chart of Accounts, beginning in 1995. While this will permit standardization, it will still be necessary to verify the quality of data, for which the departmental comptroller offices and (especially) the local governments generating the information will require strengthening.

1.40 Tax administration in most DLGs is organized around specific taxes, rather than on the basis of functions, which disrupts the smooth operation of the taxation process. Revenue divisions are generally limited to receiving and controlling payments from taxpayers, owing to the lack of effective audit programs and collection activities. Meanwhile, in an attempt to systematize certain tasks such as taxpayer registration and receipt of payments, tax authorities have delegated many responsibilities to commercial banks or outside firms, making it even more difficult to provide effective management.

1.41 Usually, the Finance Secretariat is responsible for all subsystems under the local financial administration. However, this administration is complicated in some DLGs that have a Treasurer's Office which is independent from the Finance Secretariat. In addition, there is no general consolidated budget combining central administration and decentralized agencies, nor is there a standardized accounts system for the DLGs. And finally, many reconciliations and accounting records are still being done manually.

D. International assistance for decentralization

1.42 Given the prominent nature of its decentralization, most of the Bank's projects and activities in Colombia have to do with this process. Nevertheless, the majority of loans themselves are channelled through the central government.

1.43 In the area of financing for the DLGs, a second operation is currently being prepared with Financiera de Desarrollo Territorial S.A. (FINDETER) that will include institutional strengthening to provide general support for a series of projects at the municipal level. 6/ Plans also call for participation in the fourth stage of the DRI cofinancing fund, as well as for productive investments in municipalities in which illicit crops have been eradicated under the alternative development program (CO-0196).

1.44 As well, the Bank is preparing a program for land titling and modernization of property records (CO-0157), which will improve the fiscal capacity of municipalities. Also in preparation is a loan for the transfer of secondary roads to the departments (CO-0058). Finally, a project for improving educational administration (CO-0142) is under way which has as one of its objectives to decentralize the education sector.

1.45 Among recently approved loans, the social solidarity network program (889/OC-CO) includes institutional strengthening components for municipalities with high levels of poverty. Likewise, the loan for reform of the health sector (910/OC-CO) is intended to promote the implementation of Law 100 of 1993, which will affect the delivery of health care services under the DLGs. And also, the technical cooperation in support of privatization and granting of infrastructure concessions (927/OC-CO) offers assistance to those municipalities that wish to increase private sector participation in infrastructure works.

1.46 At the same time, the IBRD has played an important role in supporting the decentralization process in Colombia through various operations in the areas of infrastructure (national highways),

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6/ Chapter IV describes the relationship between the operation proposed here and the Bank's other activities with FINDETER.

agriculture and natural resources (rural development, agricultural technology), urban development (water supply and sanitation, local financing) and social services (primary and secondary education, nutrition and municipal health services). The local financing operation with FINDETER (approved in 1991) was cofinanced with the Bank (LO-715/OC), and the two institutions are currently preparing a second stage of the program which should be approved in the first half of 1997 (CO-0138). Finally, the CAF has recently approved an infrastructure loan for education in municipalities, which is being carried out by FINDETER.

E. The Bank's strategy

1. The Bank's strategy under the Eighth Replenishment

1.47 The Bank supports efforts aimed at improving public administration in the areas of fiscal management and provision of social services, as well as in project preparation which is a requirement for more rapid development. The Bank also promotes the decentralization process through institutional strengthening and financing for the agencies responsible.

2. The Bank's country policy

1.48 In August 1995, the Board of Executive Directors approved the Country Programming Paper for Colombia (GN-1886), which sets out the Bank's strategy in this country for the period 1995-1997. This strategy was based on a study of the principal challenges that Colombia will face over the next few years, namely: (i) maintenance of macroeconomic balance; (ii) consolidation of the decentralization process; and (iii) support for the social sectors.

1.49 Hence, the Bank's strategy was organized on three fronts. First, it will support direct investment in the social sectors as a means of alleviating poverty and raising the standard of living. Second, it will strengthen the management of public institutions in order to make public spending more efficient. And third, it will encourage greater private sector participation through a series of initiatives aimed at increasing economic productivity.

1.50 The proposed operation is specifically identified in the Country Programming Paper. While this program does not entail activities specifically targeted to the social sector, promoting financial solvency and strengthening the institutions responsible for fiscal management at the subnational level are essential if DLGs are to take over the delivery of basic social services, a task assigned to them under the Constitution of 1991.

II. THE PROGRAM

2.1 During the past year, the central government received 30 requests for financing for economic reforms among other things. In order to respond to these requests systematically – rather than continue on a case-by-case basis – in April 1996 the central government approved CONPES Document No. 2843 (Program in Support of Fiscal Restructuring and Institutional Strengthening for Local Governments), in which support is requested from the Bank and the Andean Development Corporation (CAF) for the present program.

A. Objectives

2.2 The overall objective of the program is to help consolidate the decentralization process in Colombia which requires: (i) ensuring that local governments are fiscally sound; and (ii) strengthening the capacity of the central government to manage the tax system and correct fiscal imbalances at the local and departmental level.

2.3 Ensuring fiscal viability at the local level will require introducing economic reforms in the DLGs, and this in turn will require measures designed to improve public finances and reinforce the institutions responsible for tax administration, as a means of making certain that the reforms are sustainable. Also, the specific objectives in the area of institutional strengthening must be tailored to the needs of each DLG, and must seek to provide: (i) a modern tax administration, organized on the basis of specific functions and equipped with effective instruments for auditing and control; and (ii) integrated financial management systems that emphasize the role of the budget as an instrument of public policy, and promote transparency in the handling of public funds.

2.4 At the same time, the program seeks to improve the central government's capacity to manage intergovernmental fiscal relations. For this reason, it will include measures to strengthen the DAF's capacity to analyze and monitor the fiscal affairs of municipalities and department, and to provide technical assistance financed by the program. In addition, information available on DLG debt will be improved through the creation of a Registry of Debt and Guarantees (REG).

2.5 Thus, the program will create a mechanism for systematically shoring up public finances and bolstering the institutions responsible for fiscal management in the departments and local governments.

B. Description

2.6 The Ministry of Finance and Public Credit (MFPC) will head the program and provide the means for bringing about structural change

in the DLGs. To this end, a fund to be managed by FINDETER will be created for the purpose of financing the programs for modernization and reform of departments and municipalities .

2.7 Before receiving resources from the fund, the DLGs must submit a Local Government Economic Reform Plan (PRET) to a Loan Committee (CC) for approval. The beneficiaries of the program must provide assurances that they will carry out the economic reforms within their jurisdictions. With this in mind, they will be required to set specific financial performance goals and take the steps necessary to meet these targets. Funds will be disbursed to the DLGs in tranches.

2.8 The resources will be allocated through financial intermediaries (FIs) which will rediscount the loans with FINDETER and assume between 50% and 80% of the overall risk. The remaining risk will be covered by the central government through a trust created for this purpose.

1. Activities to be financed

2.9 The program is intended to fund activities aimed at restoring financial soundness and strengthening institutions within the DLGs. In addition, it includes steps to improve the management capacity of the central government in the area of intergovernmental fiscal relations.

2.10 Specifically, the program will finance activities in the DLGs that relate to: (i) administrative reforms; (ii) transfer of assets (privatization, granting of concessions, etc.); and (iii) technical assistance in tax administration, financial administration and human resources management.

2.11 At the level of the central government, resources will be used to finance: (i) institutional strengthening for the DAF, the body responsible for evaluation and supervision of the program; and (ii) creation of the REG, which is necessary to improve the quality of fiscal data at the local level.

2.12 To this end, consulting services, computer purchases, training costs and expenses associated with the transfer of assets and reductions in force will be considered eligible expenses under the program.

2. Specific activities

2.13 The following activities are planned as a means of placing the DLGs on a sound financial footing:

a. review of the organizational structure of the DLGs, including central administrations and decentralized agencies;

b. review of the business practices and operations of the DLGs and preparation of conditions for the transfer of assets;

c. provision of funding for separation packages, social benefits and, in certain instances, back-pay owed to personnel who are terminated as a result of the above reviews (this action is deemed essential for modernization of the local administrations in order to balance their budgets).

2.14 To make the DLGs financially viable will require the restructuring of the local government apparatus in each area. A smaller civil service will not only improve public finances, but also permit better use of resources and increased efficiency on the part of the DLGs. Under the mandate of the Eight Replenishment, these activities will be backed by institutional strengthening for those public sector agencies responsible for fiscal management (tax administration and financial administration). This program is also consistent with the guidelines of the Eighth Replenishment with regard to modernization of the State and deepening of the decentralization process.

2.15 In the area of tax administration, activities are planned under the following headings:

a. Regulations: review and updating of tax codes according to guidelines developed by the DAF.

b. Organizational structure and responsibilities: (i) prepare and/or update organizational manuals and job descriptions to ensure that responsibilities are clearly defined at each level; (ii) replace the current system based on specific taxes with a tax administration system based on function in which there is continuous control at all stages of the taxation process, from the registration of taxpayers to enforcement of collection procedures.

c. Management and control: (i) create a taxpayer master file system with separate modules for individual and corporate taxpayer accounts, and recording of applicable taxes; (ii) set up a current account system in which each taxpayer will have an individual account in which to record specific debits, credits, payments and balances vis-à-vis the tax authority; (iii) oversee the actions of external entities (banks) responsible for receipt of taxes; and (iv) design and put in place audit programs intended to broaden the tax base.

2.16 Actions to improve financial administration are planned in the following areas:

a. Information systems: develop and implement an integrated financial management system capable of receiving, allocating and utilizing the public resources efficiently, using an

integrated computer platform and rationalization and integration of procedures.

b. Budget: improve the quality of the budget document and develop proper evaluation mechanisms.

c. Treasury: design a master account for departmental and local governments in order to guarantee centralized financial control.

d. Public borrowing and credit: review and prepare the legal basis and procedures governing public borrowing; the issuance, placement and redemption of securities; and the repayment of debt.

e. Accounting: reorganize the accounting system and procedures used by the DLGs to ensure that they are consistent with the standards established by the DGCP, particularly with regard to the preparation of manuals, the standardized register of financial transactions, the issuance of financial statements and the integration of economic classifications.

2.17 In the area of human resources, activities will be included to:

a. assist with the design and implementation of employee separation plans as part of the restructuring activities carried out under the consolidation of public finances;

b. strengthen human resources management by modernizing rules and regulations governing contracts, licenses, absenteeism, overtime, etc., and data access systems.

2.18 The role of the DAF in the supervision of fiscal matters at various levels of government will be strengthened. This agency will be aided by a consulting firm specializing in public finance at the local level, and other areas of technical assistance. This group of consultants will in turn be assisted by DAF personnel assigned to the program, which will enable this entity to continue this function in future.

2.19 Finally, a Registry of Debt and Guarantees (REG) will be created to improve the quality of financial information at the local level. The MFPC will be responsible for maintaining this register, and for compiling the information received from Office of Banking Supervision the MFPC, and the DLGs.

3. <u>Operating arrangement</u>

2.20 This program will be governed by the Credit Regulations signed by Colombia, the Bank and the CAF. These regulations shall be approved as a condition to disbursement. A draft version of these

regulations is presented in Annex II-1. The final version will also include the contracts required for execution of the program.

C. Costs and financing

2.21 The government has provided for a fund to be established under this program for the equivalent of US$72.5 million, of which the Bank will provide US$40 million. The resources in this fund will be sufficient to finance reform programs for approximately 10 departmental and local governments.

2.22 In preparing the program, studies were conducted in a group of DLGs to cost the different components. 7/ Thus, it is estimated that the fiscal reform component will cost around US$6 million for each DLG, with the attendant costs of reductions in force accounting for the greater part of this amount.

2.23 The average cost for technical assistance for each DLG, including all possible areas of action, will be US$1 million. However, costs for some DLGs may be less than this since: (i) not all DLGs will require assistance in every area; and (ii) economies of scale are expected to result during execution of the program if similar components for two or more DLG's are managed jointly. In addition, the cost of setting up a technical support unit in each DLG to oversee the PRET is estimated at US$400,000.

2.24 The local counterpart contribution will consist of US$25 million from the CAF. In addition, a total of US$7.5 million will be appropriated from the national budget to finance the Centralized Technical Unit (UTC) and the preinvestment studies for preparation of the economic reform plans, and to fund creation of the REG.

2.25 Following is the program budget reflecting the activities described in this chapter:

7/ The fiscal situation of the municipality of Montería and the departments of Sucre, Cauca, Caldas and Atlántico was studied. The tax administration and financial condition of the first three of these entities were analyzed as well.

Table 2

Program costs
(US$ millions)

	IDB	CAF	Local Counterpart	TOTAL	%
I. Administration	2.5	1.5	5.6	9.6	13.2
1.1 Central Technical Unit	0.0	0.0	5.0	5.0	6.9
1.2 Unidad Técnica Territorial	2.5	1.5	0.0	4.0	5.5
1.3 REG	0.0	0.0	0.6	0.6	0.8
II. Direct costs	37.1	23.25	0.0	60.35	83.2
2.1 Fiscal reform	27.0	17.5	0.0	44.5	61.3
2.1.1 Studies	0.3	0.2	0.0	0.5	0.7
2.1.2 Labor costs	26.7	17.3	0.0	44.0	60.7
2.2 Institutional strengthening	10.1	5.75	0.0	15.85	21.9
2.2.1 Tax and financial administration	9.3	5.2	0.0	14.5	20.0
2.2.2 Human resources	0.8	0.55	0.0	1.35	1.9
III. Recurrent costs	0.0	0.0	1.4	1.4	1.9
3.1 Preparation of PRETs	0.0	0.0	1.4	1.4	1.9
IV. Financial costs	0.4	0.25	0.5	1.15	1.6
4.1 Credit fee	0.0	0.0	0.5	0.5	0.7
4.2 Inspection and supervision	0.4	0.25	0.0	0.65	0.9
TOTAL INVESTMENT	40.0	25.0	7.5	72.5	100.0

III. EXECUTION OF THE PROGRAM

A. Organization

3.1 In designing the program, lessons learned from the reforms at the subnational level mentioned earlier in this document were duly incorporated. As a result, it was decided to make the MFPC the ultimate authority responsible for the program. In addition, to ensure the credibility of the program, it was decided that FINDETER and the FIs should be employed as financial agents for the subloans. Similarly, a decision was made to strengthen the agencies responsible for execution of the program, at the central government level and in the DLGs.

1. Borrower and executing agency

3.2 FINDETER will be the borrower in this operation owing to its status as the government agency responsible for financing for the DLGs. The experience acquired in its local operations, combined with its position as a second-tier financing institution, makes it well-suited to this role. Accordingly, the subloans and their repayment will be handled through Colombia's financial intermediaries (FIs).

3.3 For the purposes of this program, the board of directors of FINDETER will create a Loan Committee (CC), which will have ultimate decision-making authority under the program. The members of the CC will be chaired by the Deputy Minister of Finance and Public Credit. Other members will be, the President of FINDETER, and the Assistant Director of the DNP. Each of these officers may designate an official from the next lower level of the respective institution to sit as his representative on the CC.

3.4 It will be the task of the CC to: (i) evaluate the studies and proposed economic reforms submitted by the DLGs; (ii) approve the performance pacts to be signed with the DLGs; (iii) authorize the signing of contracts between the DLGs and the financial agent; (iv) authorize disbursements and make recommendation on actions; and (v) approve technical assistance agreements in the areas of financial administration, tax administration and management of human resources.

2. The Central Technical Unit (UTC)

3.5 The government and the project team agreed that agencies in the public sector would be used to execute the program, providing them with the institutional strengthening needed for performing their duties. Consequently, the program calls for creation of an institutional coordinating body that will be called the Central Technical Unit (UTC) to be staffed with personnel from the pertinent units in the DAF and FINDETER. The creation of the UTC,

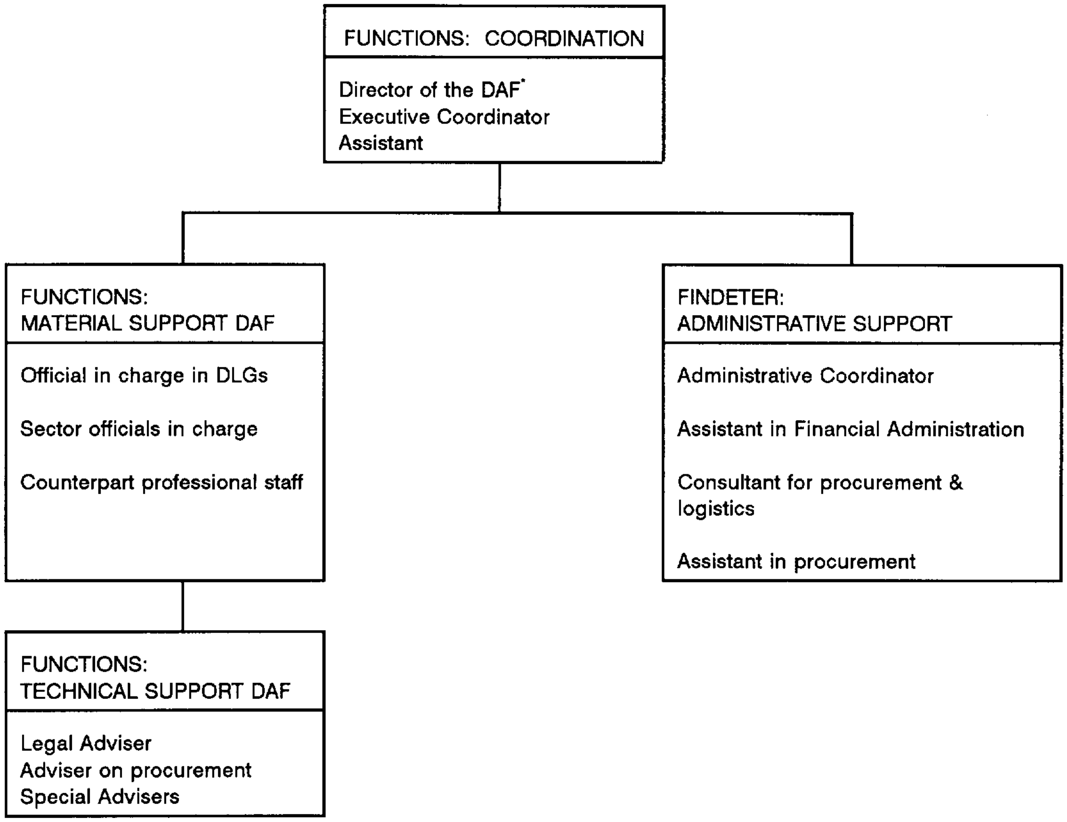
along with the appointment of its members, will be a condition precedent to disbursement of the loan.

3.6 The UTC will be headed by the Director of the DAF, and its mandate will include: (i) keeping the CC informed and reporting on the progress of the program; (ii) submitting all pertinent matters for approval by that body; (iii) coordinating activities required for approval of the program between the DAF and FINDETER; (iv) arranging for and evaluating contracts approved by the CC; and (v) making recommendations on the allocation of the necessary preinvestment resources for the program.

3.7 The DAF will oversee performance of the major program activities, creating two groups for this purpose: one to be responsible for overall monitoring of the PRETs, including areas of technical assistance and another in legal matters and contracts.

3.8 Given its experience with the administration of similar programs, FINDETER will have charge of the following: (i) administration of program finances, including verification of compliance with contractual obligations, keeping the accounting records, maintaining financial controls for the program, and preparation of requests for disbursements; and (ii) handling of contracts and logistics, including recruitment of consulting services and the procurement of goods, and logistical support for the day-to-day operations of the UTC.

CENTRAL TECHNICAL UNIT



* Full-time staff member

3.9 The UTC's operating costs, excluding full-time staff of the DAF (Director and counterpart professionals), for a period of 36 months are estimated at US$5 million. Annex III-1 contains the detailed budget of the UTC.

3. Financial agents

3.10 The FIs will act as financial agents for the program, and their presence will introduce a note of financial discipline in the granting of subloans. These same FIs will assume a proportion of the risk in the event of default on the part of the DLGs, which will range from 50% to 80% of the amount for each subloan. This percentage figure may not be less than 50% without the prior agreement of the Bank and the CAF. In discussions with the FIs, the latter indicated they tended to relate risk closely to the viability of the operation with the DLG and this would be reflected in its PRET.

4. The trust

3.11 To encourage participation by DLGs that would have difficulty accessing resources provided exclusively by an entity established under private law, the government will cover the portion of the default risk not assumed by the FIs.

3.12 To this end, the government will earmark resources from the national budget each year to cover possible losses due to nonperformance by the DLGs. These resources will be transferred to a civil law entity and administered as a fiduciary trust. The entity administering this trust will be selected from the Colombian financial system through a bidding process. Firms connected to the entity that is selected as trustee will be prohibited from participating as FIs under the program.

3.13 To obtain access to its guarantee, DLGs will sign counter-guarantees in favor of the trustee upon approval of their PRETs, as part of a series of financial requirements for the subloans. In the event of default by the DLG, the financial intermediary will draw on these resources to meet its commitment to FINDETER. At the same time, the trustee will begin proceedings for enforcement of the counterguarantees.

3.14 The creation of the trustee and establishment of the conditions for its operation will be conditions precedent to the first disbursement.

5. Eligible beneficiaries

3.15 All departments, municipal capitals and municipalities with 100,000 or more inhabitants will be eligible for subloans under the program. This makes a total of 79 local governments. The program resources are expected to be sufficient for between 8 and 12 subloans.

3.16 The group of eligible beneficiaries represents a wide range of conditions in terms of relative development, size, complexity of problems, requirements, etc., and the program's resources cannot be expected to meet all of the potential needs of eligible recipients. Consequently, a ceiling will be placed on the amount of funding available for any one DLG, making subloans more attractive to medium-sized governments than to larger ones since they will be financing a larger share of the reforms undertaken. The DLG will receive the subloan as soon as it is approved by the CC. To participate in the program, DLGs must provide a minimum of 10% of the proceeds of the subloan as counterpart funding.

3.17 The agency responsible for implementing the PRET at the local level will be the Finance Secretariat. To oversee execution of the plan, it will create a DLG Technical Unit (UTT) headed by the Secretary of Finance, who will be assisted by an Executive Coordinator. The

tasks carried out by each UTT will vary according to the scope of the PRET, and many will probably have to be delegated to local executing bodies (e.g. tax units).

6. <u>The Registry of Debt and Guarantees (REG)</u>

3.18 The REG will be established as an information system for the purpose of: (i) enabling the central government to monitor the finances of departmental and local governments; (ii) improving transparency in credit markets by improving FI capacity to evaluate commercial risk on loans to local governments. The REG will have a real-time updating system and will be accessible to the public.

3.19 The registration process will begin when the beneficiaries receive loans under this program, and a schedule will be drawn up for the registration of the other eligible beneficiaries. Given its importance as a means of ensuring participation by financial intermediaries in the program, as a condition to disbursement, it must be demonstrated that the prototype REG is up and running.

3.20 The MFPC will be responsible for maintaining the REG, receiving and updating information, and compiling results. The information itself will come from three sources: the Office of Banking Supervision, the MFPC, Government Accounting Directorate and the DLGs. The Office of Banking Supervision (SB) will issue a circular to all FIs specifying the data format to be used.

3.21 The REG will contain primarily the data from existing loan agreements with DLGs eligible under the program, making it possible to calculate the amount owed by each government. This information, in turn, can be used to forecast the financial flows of the DLGs. As well, both FIs and the DLGs must provide data on the income flows securing these loans.

B. <u>Execution</u>

3.22 In order to participate in the program, local governments must draw up a Local Government Economic Reform Plan (PRET). This plan will include a diagnostic study of the current circumstances faced by the DLG, by its central administration and its decentralized agencies, and a number of goals and activities proposed for remedying the situation. This document will be submitted to the CC for analysis and approval. The administration of the DLG will be required to have the authorization of the Legislative Branch in order to participate in the program.

3.23 The goals and activities contained in the PRET will be of two major types. The first will comprise measures for fiscal reform, with the goal of achieving a surplus in the primary operating budget and controlling the rise in its debt load. This group of activities will be aimed at fundamental economic reform, and will include

restructuring of agencies and a reduction in personnel costs, to be supplemented by specific measures in the area of taxation.

3.24 The second group of activities will be designed to provide institutional strengthening for governments in the areas of taxation (tax administration and financial administration) and human resources management. The nature of these institutional-strengthening activities will determine the duration of the PRET. This group of activities is necessary to ensure the sustainability of DLG economic reforms.

3.25 A subset of goals and activities set out in the PRETs will be incorporated into a matrix of conditions to monitor the subloans granted to the DLGs (see Annex III-2). Selecting a limited number of goals and activities will make it possible to adopt uniform policies for the DLGs, focus on substantive aspects of the program, and improve their administration.

3.26 When a PRET receives approval from the CC, the local government, FINDETER and the MFPC will sign a performance pact setting targets for the DLGs. The departmental or local government, FI and trustee will sign the necessary documentation (loan contracts, guarantees and counterguarantees to cover the amount of the financing) required for rediscounting the resources with FINDETER.

3.27 The CC will authorize the transfer of resources to the DLG when all supporting documents have been completed and the conditions precedent to the first disbursement have been met. After this, the CC will proceed to authorize disbursements as fulfillment of the conditions set out in the matrix are verified.

3.28 Implementation of the PRET will restore fiscal viability to the DLG by increasing revenues and reducing expenditures. This will improve the liquidity of the guarantees posted by the DLG, so that provision has been made for FIs to alter their exposure while the subloan is in effect.

3.29 The guarantees and counterguarantees provided by the DLGs are to be executed by the FIs and the administrator of the trust, respectively, in the event of default in debt-service payments, in accordance with the regulations of the SB. In addition, the CC can demand early repayment of all or part of the subloan for nonperformance of commitments (activities, debt-servicing, supply of information, etc.) on the part of a departmental or local government.

C. Financial conditions

3.30 The IDB loan will be in United States dollars; accordingly the Government of Colombia will have recourse to the Single-Currency Facility.

3.31 The financial spread for FINDETER in foreign exchange operations discounted with commercial banks will be 1.5 percentage points.

3.32 For their part, the financial intermediaries will be allowed a spread of between 2 and 5 percentage points, depending on the level of risk assumed. FIs that decide to assume 50% of the risk, with the trustee covering the other 50%, will be permitted a spread of 2 percentage points. An FI willing to assume 80% of the risk will be allowed a maximum mark-up of 5%. FIs will be permitted to increase the percentage of risk they assume, if their perception of the overall amount of risk changes during the life of the loan. The spread which FIs are allowed to charge may be changed by the CC — subject to both the Bank's and the CAF's nonobjection — based on the results of the mechanism proposed for this program and in keeping with FINDETER's policies.

3.33 The DLGs will be charged interest in United States dollars, at a variable six-month rate based on the weighted cost of loans for the Bank and the CAF, for a maximum of 8 years with a two-year grace period. The resulting overall interest rate, including operating costs of the national government and the spreads for FINDETER and the FIs, will vary between 13% and 15%. These rates are similar to those offered on the domestic market for comparable operations.

D. Execution period

3.34 The resources under this program will be committed within a period of 18 months following the date on which the loan contract is signed, and it is estimated that they will be disbursed within a period of not more than 42 months reckoned from that same date. The date for commitment of resources is defined as the date on which the loan contract is signed between an FI and the departmental or local government. Submission of tentative schedules for (i) preparation of PRETs and (ii) disbursements to DLGs will be a condition precedent to the first disbursement of Bank resources under this program.

E. Recognition of expenses and project preparation advance

3.35 A number of activities carried out under this program will have a high political cost, particularly those related to reductions in force. To minimize these costs, it is recommended that the equivalent of up to 20% of the total amount of the loan (i.e. up to US$8 million) be advanced to FINDETER for project preparation. Subsequent disbursements are to be made upon request by FINDETER at the intervals specified, with proper justification.

3.36 It is not expected that counterpart resources will be disbursed in advance of the date scheduled for approval of this loan by the Bank's Board of Executive Directors (December 4, 1996).

F. Monitoring, evaluation and progress reports

3.37 The MFPC, FINDETER, the CAF and the Bank will meet every six months to review the project during the disbursement period of the loan. At these meetings, the results achieved under the program will be presented and its operation evaluated to see if changes are needed to facilitate its implementation. After completion of the disbursement period, further meetings will be scheduled in consultation with the MFPC to assess the impact of the reforms implemented.

3.38 Annex III-2 lists the indicators for monitoring performance of the PRETs, compliance with which will determine the disbursement schedule. Finally, the logical framework for the program is set out in Annex III-3.

3.39 The UTC will prepare the progress reports required for periodic evaluation of the program. To this end, the UTC will draw up quarterly reports, updating the information relating to beneficiaries, compliance with prerequisites for disbursement, utilization of resources and the fiscal results achieved.

G. Procurement procedures

3.40 The program does not call for infrastructure works other than refurbishing of premises required for implementing the activities of the PRETs. For procurement of related goods and services, it is recommended that international competitive bidding be used for contracts valued at the equivalent of US$350,000 or more. For consulting services, the threshold proposed is US$200,000. For procurement below these amounts, contracts will be awarded in accordance with Colombian legislation. Annex III-4 contains a table summarizing the procurement schedule for this operation.

3.41 The Bank's procedures contained in Annex C will be followed for the hiring of consulting services. It is expected that a registry of consultants will be established, and updated by means of prequalification notices published annually. Contracts will be awarded to consultants on the registry by the short procedure. The Bank and the CAF must express their nonobjection to the terms of reference for consultants.

H. External auditing

3.42 Financial statements for the program during program execution period, and those of FINDETER for the duration of the loan will be submitted each year to the Bank. The statements must be duly audited by an independent firm of certified public accountants acceptable to the Bank.

I. Final evaluation

3.43 With a view to the possible introduction of improvements and expansion of the program to include a larger number of DLGs, a final evaluation of its results will be done six months after the final disbursement. The semiannual evaluations prepared during the disbursement period will serve as the basis for this final evaluation — especially as some DLGs may have fulfilled the provisions of their performance pacts before the date of the final disbursement.

IV. BORROWER AND EXECUTING AGENCY

A. The borrower

4.1 The borrower and executing agency for this program will be Financiera de Desarrollo Territorial S.A. (FINDETER), an independent agency created in 1990 under Law 57/89 having legal personality and its own equity base. The legal representative of the agency is its President, who is appointed by the President of Colombia and is responsible for the administration of FINDETER.

B. The executing agency

1. Nature and objectives

4.2 FINDETER was designed and created as part of the political and administrative process of decentralization introduced by the Colombian authorities. Its mandate is to provide technical and financial support for the country's local governments, supplying them with medium- and short-term debt financing by rediscounting loans from commercial banks. Under its charter, FINDETER is not permitted to act as a first-tier bank and must carry out its debt financing operations through the nation's financial intermediaries.

4.3 Under its statement of corporate purpose, FINDETER is required to perform the following functions: (i) discount loans granted by banking establishments to local governments for investment projects of the kind defined in its statement of corporate statement; (ii) attract domestic savings by means of financial instruments or contractual arrangements; (iii) accept fixed-term or demand deposits from public agencies, in exchange for payment of the corresponding consideration; (iv) external credit transactions; (v) enter into trust, guarantee, agency or payment contracts; and (vi) act as trustee for resources transferred from other public agencies to finance programs related to its corporate purpose.

4.4 Under Law 57/89 creating FINDETER, its board of directors must authorize this program, declaring it to be in accordance with the agency's corporate statement. This authorization must be granted prior to the signing of the loan contract. This will enable FINDETER to discount loans in foreign exchange to finance operations with DLGs undertaking fiscal reform and institutional strengthening.

4.5 Notwithstanding FINDETER's status as an autonomous agency, it remains formally linked to the central government through the MFPC, the minister of which (or his delegate) serves as Chairman of the board of directors of FINDETER. The central government controls FINDETER's operations inasmuch as: (i) its President is appointed by the President of Colombia; (ii) the national government holds at

least 80% of its equity stock; and (iii) the President of Colombia has the power to amend its charter.

2. Share capital

4.6 FINDETER is a financial corporation registered at the national level with majority ownership by the central government (91.91%), with contributions from 29 departments (7.82%) and INFINORTE a decentralized government agency (0.27%).

3. Capital structure

4.7 As of July 31, 1996, FINDETER had an authorized capital of Col$200 billion (US$192.3 million), divided into 2 million share with a par value of Col$100,000 each. In December 1994, 671,113 shares were subscribed and fully paid up; by June 1995, this figure had risen to 884,354 shares; and by July 1996, there were 1,049,208 shares subscribed and fully paid up.

4. Organization and operations

4.8 FINDETER has an organizational structure consistent with its legal status and function as a specialized financial agency. The shareholders and the board of directors are responsible for the management of the company. FINDETER's organizational structure is shown in Annex IV-1.

4.9 The board of directors has the following members: (i) the Minister of Finance and Public Credit or his authorized representative, as Chairman; (ii) the Minister of Economic Development or his authorized representative; (iii) the Secretary of Economic Affairs for the Office of the President of the Republic; (iv) the Director of the DNP or his alternate; and (v) two representatives from the DLGs, with their respective alternates.

4.10 The senior management consists of the Chairman, two Vice-Chairmen (Finance and Projects), and the General Secretariat. The following middle-management positions exist: (i) a National Regional Coordinator who is responsible for the 10 regional units into which Colombia is divided; and (ii) six heads of operating divisions. Reporting directly to the Chairman are: (i) the offices of planning, information systems and internal controls; and (ii) the Directorate for Cofinancing Operations. FINDETER has currently budgeted for 213 positions, 96 of which are assigned to regional units, while 117 are employed at headquarters in Bogotá. There are two technical committees and two loans committees to assist with loan approvals (one departmental and one national).

4.11 Due to the nature of the program proposed in this document, FINDETER will create a Loan Committee (CC) whose task will be to approve subloans to local governments under this program.

5. Systems of control, audits and accounting

a. Internal controls

4.12 The Office of Internal Controls will be responsible for judging the suitability, relevance and sufficiency of the internal controls used in the agency's administrative, operational and technical procedures. Also, it will advise senior management on the continuity of the processes, the reassessment of its established plans, and the introduction of corrective measures to produce greater efficiency and to achieve its goals.

b. External controls

4.13 External control, inspection and supervision corresponds to CONPES, the Office of Banking Supervision (SB) and the Comptroller General's Office (CGR) – each within its area of competence. CONPES determines the government's social and economic policies, and its decisions concerning regional development directly affect FINDETER. The SB is a technical agency responsible for inspection and monitoring of transactions in the nation's financial system, in particular those of FINDETER as a special institution that finances regional development. Finally, the CGR conducts an annual audit of the financial statements of government agencies such as FINDETER from the previous year.

c. Accounting

4.14 FINDETER's policies regarding accounting and the preparation of financial statements are subject to accounting principles established by the SB, in particular the provisions of the Standard Chart of Accounts for the Financial Sector which permits standardization of practices and accounts throughout the financial sector.

d. Auditing

4.15 Because of its corporate status, FINDETER is subject to the provisions of the commercial code, and is therefore required to appoint a statutory auditor. Compañía Nacional Ulloa Garzón y Asociados Ltda., correspondent firm of *Grant Thornton International*, conducts audits of FINDETER's financial statements and operating results.

6. Loan policies

4.16 Among the general policy criteria governing FINDETER's credit operations are the following: (i) maintaining financial spreads that are sufficient to ensure self-supporting operations; (ii) application of borrowing and lending rates that are consistent with those in the financial market; and (iii) use of flexible

mechanisms that promote competition among financial intermediaries for access to its resources.

4.17 FINDETER's lending activities are governed by the provision of Resolution No. 43 issued by the Board of Directors of Banco de la República in 1990, as well as by the policies set in this regard by FINDETER's own board of directors. The conditions governing FINDETER's operations in the area of interest rates are consistent with the current regulations which pertain to the financial sector and which have significantly reduced the distortions that have played havoc with this sector in the past.

4.18 As a consequence, the interest rate currently applied by FINDETER on rediscounts granted to the FIs is 2.5 percentage points above rate on certificates of deposit (CD). The CD rates fluctuate daily based on supply and demand for financing in the credit market.

4.19 For their part, the FIs that rediscount loans with FINDETER offer rates up to a maximum of 5 percentage points above that paid on CDs. The exact amount of the spread is set by each FI on the basis of how competitive its loan resources are on the country's credit market at the time the loan is signed with the borrower.

4.20 The FEDESARROLLO Foundation is conducting a study as part of the preparations for the second stage of a regional funding program to be cofinanced by the IDRD and the Bank (CO-0138). In this study, FINDETER's financial policies will be reviewed, particularly the actual level of spreads it has applied and the means for determining same. It is likely that this study will result in changes to the current spreads, and that it will recommend the elimination of the ceiling on spreads so that these can be freely determined by the market.

4.21 As mentioned in chapter III, the spread which FINDETER will apply to the foreign exchange transactions it discounts for the FIs under this program will be 1.5 percentage points. This margin will enable FINDETER to cover its overhead costs and the risk associated with the rediscounting of debt.

7. The program and other Bank activities involving FINDETER

4.22 The Bank has taken a very active role in regional development in Colombia through various loans with Banco Central Hipotecario (BCH) and its successor FINDETER. The specific objective of operations with the BCH was to provide long-term financing for urban development works in small and medium-sized municipalities, primarily to benefit low-income population groups. FINDETER itself has been the recipient of two loans from the IDB: one reimbursable technical-cooperation program, the object of which was to provide institutional strengthening for FINDETER along with specific technical assistance projects for small and medium-sized

municipalities; and one global credit operation for a municipal development program (PDM) cofinanced with the World Bank.

4.23 PDM-I has provided pivotal support for Colombia's decentralization process. In addition to promoting participation by private sector FIs in the financing of municipal works, the PDM has provided specific technical assistance for municipalities in various areas, particularly with respect to municipal administration and the preparation of projects. During phase two of the PDM is currently being prepared in which a strategic study will be carried out to determine the future role of FINDETER, with the aim of promoting development of a municipal bond market, and to explore new financing instruments that FINDETER might develop to lessen its reliance on rediscounting. In addition, the study will determine what type of technical assistance FINDETER should be providing for the DLGs in its new role.

4.24 The proposed program, while contributing to Colombia's decentralization efforts as did the Bank's earlier operations in that country, will add a new dimension of support and reinforcement for the DLGs by establishing a mechanism to help with fiscal reform and institutional reform in taxation and financial administration. Consequently, the present program will contribute to the effectiveness of the other actions carried out by the Bank under PDM-II (CO-0138).

8. Financial status

4.25 FINDETER's financial status and overall performance as of July 31, 1996, is set out in Annex IV-2, based on financial statements audited by an independent firm of certified accountants.

4.26 Analysis of these financial statements shows that FINDETER is in sound financial condition, with reasonable financial management ratios. Following are the most relevant results of the analysis of its overall balance sheet:

a. The total current assets of the Fund are equivalent to US$440.4 million, with the rediscounted portfolio accounting for 87.3% of this total (equivalent to US$384.4 million). As this portfolio consists entirely of transactions with commercial banks and other credit institutions, the risk of default in virtually nil.

b. The larger part of its liabilities (which total the equivalent of US$185.4 million) is in either bank loans (IBRD: US$112.5 million; IDB: US$20.0 million; and others: US$3.9 million) or debt securities, which are two of the instruments it uses to raise funds. During the period 1991-1995, bank loans increased in nominal terms at an average 28.6% annually, whereas debt securities fell (again, in nominal terms) by an average 14.6% per year.

c. Net worth (US$255 million) is equivalent to 58% of total assets, with liabilities (US$185.4 million) being covered by the remaining 42.1%. This means that debt-to-equity ratio continues to hover around 0.7, a relatively low ratio for this type of institution.

4.27 The statement of earnings shows that during the fiscal year ending on July 31, 1996, FINDETER:

a. earned pre-tax profits equivalent to US$18.5 million which – after income tax – resulted in a net gain equivalent to US$12 million. This figure represents a return on equity of 4.7%, and 11.4% on shareholder's equity of 11.4%, reasonably high figures;

b. achieved a gross financial margin of approximately 1.38% on its total rediscount portfolio plus investments in securities;

c. incurred total overhead and personnel costs equivalent to US$7.3 million, or 16.4% of total income and 1.8% of the consolidated balance of its rediscount portfolio and securities. Operating ratios such as these are considered reasonable.

C. The Fiscal Support Directorate (DAF)

4.28 The DAF is a branch of the MFPC with a mandate to promote decentralization of both fiscal operations and development of financial regulations. Its organizational structure is made up of the Director's Office, support and technical units and an administrative coordination division.

4.29 In the last few years, the support which the DAF has provided for the decentralization process has been in the form of help for the departmental and municipal authorities, primarily in the area of tax and financial administration. This support has consisted of responding to queries from DLGs (roughly 500 per year) and provision of training. Also, the DAF helped prepare the bill on DLG borrowing which is currently being debated by Congress, and is helping to draft reforms for the departmental and local government tax system.

4.30 The DAF has a personnel roster of 29 professional positions (22 of which are currently filled) and 16 administrative and support positions. The DAF's present professional staff is not qualified for the mission that the Directorate is expected to carry out, nor is the level of remuneration sufficiently attractive to attract specialists in fiscal administration and financial management.

4.31 Using counterpart funds provided under the program, the required specialized personnel will be hired in the areas of DLG finance and

in areas financed with the technical assistance. In all cases, the hired personnel will be assigned counterpart staff members from the DAF.

V. FEASIBILITY, BENEFITS AND RISKS

A. Feasibility

5.1 The proposed program involves a relatively novel approach, both for the Bank and for Latin America as a whole. Successful implementation could lead to additional demand, not just in Colombia but in other countries undertaking decentralization and regional or local development as well.

5.2 The approach taken up to now in attempting to consolidate public finances in Colombia (in the departments of Chocó, Nariño, Putumayo and La Guajira) has run into a number of problems that have detracted from the viability of this type of operation. Among other things, programs have responded to general crises on a case-by-case basis without developing a coherent strategy based on sound fiscal policies. In addition, the response has been immediate without taking the necessary time to develop a complete diagnosis and adequate measures for overcoming the structural problems of these departments. Finally, incorrect information was supplied concerning their financial conditions and the mechanisms for the recovery of loans.

5.3 The feasibility of the proposed program is based on a series of elements that were taken into account in preparing for this operation. In the first place, the role of the MFPC has been bolstered in the planning and implementation of the program, both in its conceptual design and within its institutions. In particular, the capacity of the DAF to monitor and evaluate progress will be strengthened, and loans will be rediscounted by FINDETER, a well-known institution highly respected by the DLGs. And in the second place, loans will be granted by the FIs (and at current market rates) in order to minimize the likelihood of defaults in their repayment. Finally, the involvement of the DLGs has been redoubled in that they are not only responsible for drafting and obtaining approval of the economic reforms, but are also required to fulfill and monitor compliance with the performance pacts.

B. Benefits

5.4 Carrying through on government decentralization is one of the objectives laid down in Colombia's constitution, and its achievement will have a positive impact both on the country's ability to provide social services, and on the willingness of its citizens to participate in the decision-making process.

5.5 The program proposed here will aid in the consolidation of the decentralization process. Specifically, it is designed to strengthen local governments by modernizing their institutions,

consolidating public finances and enabling them to balance their budgets. Since the DLGs cover most of the country's spending on social sectors, the program is also expected to result in greater efficiency in the delivery of social services. As well, the strengthening of the DLGs' institutions will strengthen the State's presence in areas where, traditionally, there has been little respect for the public authorities.

5.6 Moreover, the program will strengthen the technical capacity of the DAF, and upgrade and improve the leadership capacity of other institutions in the central government. This increased leadership by the central government will be accompanied by a systematic attack on fiscal deficits at the local level, which will give greater transparency and credibility to both the institutions themselves and the mechanism employed.

5.7 As a further plus, restoring the regions affected to financial soundness will directly benefit the local governments, as well as reestablish fiscal balance throughout the country.

5.8 Finally, creation of the REG will likewise help to generate timely and reliable data on taxes levied by DLGs. This will have a positive effect on fiscal administration at the central and regional levels, and on efforts to ensure transparency in FI lending.

C. Risks

5.9 The main risk associated with this operation has to do with the sustainability of the reforms. The success of these initiatives is closely related to the political support that they receive from governors, mayors and local legislative bodies. A change in political leadership at the local level could signify a possible reversal of the reforms.

5.10 The monitoring and oversight duties of the Central Technical Unit to be created under this program is therefore vital. And to further mitigate this risk, financing for the program will be disbursed in tranches to reduce the possibility of improper use of resources.

5.11 Another risk stems from the participation of FIs in the program, and the possibility that some beneficiaries may turn out to be poor credit risks. To counter this risk, the government established a trust covering from 20% to 50% of the amount of each loan. In addition, the Loan Committee (CC) will be empowered to change the financial spreads in the event that these prove inadequate for ensuring participation by the FIs. Lastly, a registry of debt and guarantees will be created in order to provide the FIs with the information needed for properly analyzing the risks involved in the operations.

CREDIT REGULATIONS

I. INTRODUCTION

1.1 These Regulations establish the terms and conditions governing the Program for Support of Fiscal Reform and Institutional Strengthening Departmental and Local Governments (hereinafter the program), to be carried out by Financiera de Desarrollo Territorial Sociedad Anónima (hereinafter called FINDETER S.A.) with the rediscounting of loans to departments and municipalities (referred to collectively as departmental and local governments or "DLGs") through commercial banks and domestic financial institutions (hereinafter called the financial intermediaries or "FIs"), using resources provided in the first instance by the Andean Development Corporation (CAF) and the Inter-American Development Bank (IDB), together with local counterpart funding.

II. OBJECTIVES, DESCRIPTION AND PROGRAM COMPONENTS

A. Objectives

1. Overall objective

2.1 To provide support for the decentralization process by financing efforts to consolidate public finances and strengthen institutions in DLGs willing to take steps to restore fiscal soundness.

2. Specific objectives

2.2 The specific objectives of the program are to:

a. Rationalize and restructure the DLGs in line with their legal mandates and potential for generating own revenues.

b. Strengthen the capacity of DLGs to generate own revenues through modernization of their tax administrations.

c. Improve management in the DLGs through financial administration programs and other systems.

B. Description of the program

2.3 The program consists in the provision of financing for DLGs that agree to draw up and execute a departmental and local Government Economic Reform Plan (PRET) which will make it possible to balance

their budgets and become more efficient in their fiscal operations and administration.

2.4 The program has two components:

a. *Fiscal reform*, designed to eliminate the deficits in DLGs that meet the eligibility criteria and undertake to prepare and carry out a PRET; and

b. *Institutional strengthening*, seeks to support the above by enhancing the financial and administrative capacity of the DLGs via provision of technology, training activities and consulting services.

2.5 DLGs applying for resources under the public finance component must at the same time agree to take part in the institutional strengthening component. However, DLGs wishing to apply under the latter component only can obtain financing for institutional strengthening without carrying out the fiscal reform component, provided they demonstrate that their government does not need to do so.

2.6 DLGs potentially eligible for the program will be able to obtain loans from the central government for carrying out the basic studies (institutional and financial diagnoses) and detailed design of the PRET. If they qualify as a result, such loans will be repaid out of the first disbursement under the subloan.

2.7 The activities to be financed under each component of the program are listed in section IV of these Regulations.

III. CRITERIA FOR LENDING TO DEPARTMENTAL AND LOCAL GOVERNMENTS

A. Eligibility criteria

3.1 The departments, municipal capitals and major municipalities with 100,000 or more inhabitants that meet the following legal criteria and satisfy requirements governing institutional commitment and the technical and financial conditions, will be eligible for subloans under the program.

B. Legal criteria

3.2 The pertinent legal criteria are that DLGs must:

a. Be in compliance with laws and regulations governing public debt.

b. Have been expressly authorized to participate in the program by the department's Legislative Assembly or the local Municipal Council, as the case may be, through passage of a resolution or ordinance approving the issuance of a new or expanded debt quota and empowering the governor or mayor to sign the respective subloan contract and performance pact, and to provide the required guarantees.

C. Institutional commitment

3.3 The institutions of the DLG must provide assurances that they:

a. Will carry out the reforms specified in the PRET and relating to their organizational structure, staffing levels or processes and procedures, and designed to improve fiscal and administrative efficiency. These activities will be spelled out in the performance pact (see section V and Attachment 1.B to these Regulations).

b. Have obtained approval of the PRET from the respective Assembly or Council, to form the basis for preparation of its performance pact.

D. Technical and financial criteria

3.4 When submitting a formal application to the Loan Committee that will evaluate their PRETs, DLGs must include information describing:

a. The current situation and problems that require solution; the organization of their central administration; current staffing levels in each branch, including vacancies and indicating duties, level and grade; payroll costs, including social security and employee benefits for all public servants and employees. 1/

b. General set-up of decentralized government agencies; mandate and objectives of each agency; earnings and operation costs; own revenues; financing costs; existing personnel roster, including vacancies, duties, level and grade for each division of the enterprise.

c. The objectives proposed by the DLGs in regard to: (i) restructuring the local administration; and (ii) development of means for ensuring more efficient

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1/ Where there are additional personnel attached to a departmental or local government under other contractual arrangements, the number, branches in which they work, salary costs and sources of funding must be indicated.

allocation and utilization of public funds, and for upgrading its planning process and management capacity.

d. Estimated cost of implementing the PRET.

e. The financial situation it hopes to achieve by carrying out the PRET, including the impact and benefits this will have.

f. An indication of how execution of the PRET will ensure the financial viability of the DLG.

IV. FINANCING TERMS AND CONDITIONS

A. Amount and financing of the program

4.1 The initial funding for the program will be approximately US$65.0 million, plus resources allocated by the national government for this same purpose. The external sources of credit will include:

SOURCE	AMOUNT (US$ millions)
CAF Loan	25.0
IDB Loan	40.0
TOTAL	65.0

4.2 This program may be expanded in future with additional contributions, depending on the progress achieved. Under program guidelines, 85% of these resources will be allotted to the fiscal reform component, and the remaining 15% to the institutional strengthening component.

B. Beneficiaries

4.3 The beneficiaries will be those DLGs that apply for subloans, and that meet the eligibility criteria established for the program and all additional requirements requested by the Loan Committee and the FIs.

C. Disbursement procedures

4.4 The resources under subloans will be transferred to the DLGs by FIs using the rediscount mechanism.

4.5 The rediscount given by FINDETER S.A. will be for 100% of the subloan approved for a given DLG.

4.6 The DLG will open a special account from which it may freely draw on the resources provided under the subloan for execution of its PRET.

4.7 Subloans will be disbursed in three (3) tranches based on progress in carrying out scheduled activities, in accordance with the matrix of conditions which forms an integral part of its performance pact.

4.8 If the employee separation and rationalization plan contained in the PRET has been completed before the third tranche, the Loan Committee may authorize disbursement to cover the total cost of the plan. In this case, a means will be devised between the Technical Unit and the financial intermediary for ensuring proper application of the resources.

4.9 In order to provide timely support for the DLGs in executing their PRETs, each tranche will be disbursed as an advance with due justification and verification of proper application. DLGs will have up to ninety (90) days, reckoned from the date they receive an advance under the subloan, in which to provide the Technical Unit with proof to substantiate application of the funds. Annex.... contains the instruments to be used for requesting and substantiating advances.

4.10 Any balance remaining from one tranche will be deducted from the amount disbursed in the following tranche. If any balance remains in the account following substantiation of the final disbursement, this amount will be reimbursed to the financial intermediary, which will arrange for its return to FINDETER S.A.

4.11 Each tranche disbursed in accordance with the matrix of conditions may total up to 40% of the full amount of the subloan approved for the DLG. In turn, each tranche will be disbursed in two or more payments, none of which may exceed 50% of the total amount of that tranche.

D. Application of funds and eligible expenditures

4.12 The resources provided under this program will be used solely for consolidation of public finances and institutional strengthening activities aimed at ensuring the immediate and medium-term financial viability of the DLGs, and improving their capacity to generate and manage revenues.

1. Eligible expenditures under the fiscal reform component:

   a. Compensation for civil servants and official employees of the central administration displaced as a result of restructuring programs or opting for separation package.

   b. Accrued salaries and wages payable by the DLG to personnel opting for separation packages or affected by redundancies.

   c. Other liabilities or payments associated with the restructuring process and privatization of government enterprises, which the Loan Committee deems necessary to meet the objectives set out in the PRET.

2. Eligible expenditures under the institutional strengthening component:

   a. The cost of preinvestment studies needed for: (i) formulating the PRET and estimating the cost of its activities aimed at balancing the budget and improving the operations of the DLGs, and preparing the plan of activities and disbursement schedule under the subloan; and (ii) determining the value of assets to be sold off, where applicable.

   b. Training for staff of the DLG in tax administration and methods of financial management.

   c. Consulting and computer services in areas directly related to execution of the PRET.

   d. Design, organization and development of tax processes and procedures consistent with current laws and regulations.

   e. Acquisition of software and hardware for modernization of tax administration and financial management.

   f. Refurbishing of facilities required for institutional strengthening activities.

E. Restrictions and limitations on subloans

4.13 The following restrictions and limitations shall apply under these regulations:

1. Restrictions

4.14 Program resources may not be used to:

   a. pay interest or principal on debts held by the DLGs;

b. make payments to personnel or cover labor costs in job categories eligible for resources from the transfers ordered by Law 60 of 1993, Law 141 of 1994 (Law on Bonuses), Law 100 of 1993, or Regulatory Decree 1893 of 1994;

c. make payments to personnel or cover any other expenditures incurred by government enterprises providing residential utility services;

d. pay back wages to any staff member who continues in the employ of the DLG after separation has been implemented;

e. effect partial payment of employee benefits requested by personnel in active service, whether with the central administration or a decentralized enterprise;

f. cover investment commitments made by the DLG under its development plans;

g. cover transfers to the decentralized enterprises of the DLGs, except in connection with the restructuring and privatization activities referred to under IV(D) above;

h. purchase fixed assets for the DLG;

i. cover costs not specified in the PRET approved by the Loans Committee; or

j. deposit amounts in banks, financial institutions or investment firms for a term of more than sixty (60) days.

2. Limitations:

4.15 Any subloan that requires the posting of a sovereign guarantee through the trust mechanism in an amount exceeding 50% of the respective loan, will be submitted to the multilateral lending agencies by the Loan Committee with a request for a statement of nonobjection, along with supporting technical and financial studies. The multilateral lending agencies will agree on common criteria and means for deciding such cases.

F. Maximum amount for subloans

4.16 Program resources may be used to finance up to 90% of the total cost for executing the PRET, so that the DLG is required to allocate counterpart funds equivalent to at least 10% of this cost. This counterpart contribution must be applied during the execution of the subloan, with the DLG guaranteeing compliance with this pari-passu requirement at the close of that period.

4.17 Following are the maximum amounts to be provided under each component:

a. Fiscal reform and institutional strengthening components: up to US$8 million.

b. Institutional strengthening component only: up to US$1.5 million.

c. To be charged against the subloan for preparation of diagnostic studies and formulation of the PRET (preinvestment costs): up to US$100,000. 2/

G. Completion schedule and amortization period

4.18 Subloans that are approved will be subject to the following completion deadlines: (i) up to 90 calendar days for submission of the first request for disbursement; and (ii) up to 24 months for completion of all activities. Completion period in both cases will be reckoned from the date on which the subloan contract is signed with the respective performance pact duly incorporated as an annex.

4.19 Subloans to DLGs must be repaid over a period of 8 years, with a 2-year grace period.

H. Currency

4.20 Subloans will be disbursed to DLGs and repaid by them in United States dollars.

I. Interest and commissions

4.21 Program resources will be transferred to the DLGs on the basis of the total cost of same, including administrative fees of FINDETER S.A. and operating costs for the financial intermediaries. The Loan Committee will conduct the necessary studies to determine cost and additional margins on resources from the foreign loans.

J. Guarantees

4.22 Each subloan granted to an DLG will be guaranteed as follows: (i) not less than 50% of the risk to be guaranteed by the FIs with easily convertible liquid guarantees, in percentages established under applicable legislation (eligible guarantees include fiscal and nonfiscal revenues not subject to a specific appropriation under current law, unless such appropriation allows the use of

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2/ Funding of preinvestment costs will be applied against the ceilings established for fiscal reform and institutional strengthening components.

resources to be applied as required under this program); and (ii) the portion of risk not guaranteed by the FIs will be covered by means of a trust fund set up for this purpose by the central government (in this case, the counter guarantees permitted under current legislation will be required, to be replaced by easily convertible liquid guarantees as the latter is generated). In exceptional cases, the provisions of IV.E.2 of these regulations will be applied.

K. Utilization of amounts repaid by borrowers

4.23 Amounts repaid under subloans will be used to pay obligations contracted by FINDETER S.A. with the multilateral lending agencies and/or to grant new subloans.

V. PERFORMANCE PACT

5.1 The performance pacts signed between the Ministry of Finance and FINDETER S.A. on the one hand, and the DLGs on the other hand, will form part of the subloans and will (in general terms) consist of the following: (i) basic principles and objectives of the PRET; (ii) activities to be carried out and specific commitments made by the DLGs, including fixed deadlines for the achievement of goals and indicators; (iii) commitment by FINDETER S.A. and FIs to make disbursements in tranches and only upon execution of the activities in accordance with the matrix of conditions attached to the performance pact; (iv) establishment of criteria and indicators for supervision, monitoring and assessment of progress in carrying out the actions listed in the pact.

5.2 The performance pact will cover a period equal in duration to that of the subloan contract. Annex.... contains a model performance contract and matrix of conditions.

VI. SPECIFIC OBLIGATIONS AND DUTIES

A. Loan Committee

1. Membership:

6.1 The Loan Committee will be made up of the following:

a. The Deputy Minister of Finance and Public Credit (or his authorized representative), who will serve as Chairman.

b. The Assistant Director of the National Planning Department (DNP), or his authorized representative.

c. The President of FINDETER, or his authorized representative.

NOTE: An authorized representative must be from the rank immediately below that of the official designating a representative.

2. Duties:

6.2 The Loan Committee is responsible for ensuring compliance with program objectives and will, among other things, be required to:

a. Set policies and criteria for awarding subloans.

b. Approve these Credit Regulations in joint consultation with the multilateral lending agencies taking part in the program.

c. Issue final decisions for approval of applications for subloans and performance pacts. The Loan Committee will decide which cases require approval by the multilateral lending agencies.

d. Establish the financing terms and conditions for subloans based on total costs.

e. Approve PRETs, performance pacts and draft contracts for subloans.

f. Determine the criteria for recruitment of consultants required to carry out the institutional strengthening component.

g. Establish the necessary mechanisms for monitoring compliance with commitments made in the performance pact, evaluating progress under same, and recommending appropriate action.

h. Approve the methods designed by the Technical Unit for creating the Registry of Debt and Guarantees in which to record the debts and guarantees issued by the DLGs.

i. Approve the organizational structure and annual budget of the Technical Unit, and supervise its activities.

2. Central Technical Unit

6.3 The program will have a Central Technical Unit which will be made up of members of the Ministry of Finance's Fiscal Support Directorate (DAF) and FINDETER S.A., and which will act in accordance with guidelines laid down by the Loan Committee. The principal duties of this unit will be to:

a. Analyze preliminary requests for subloans submitted by DLGs and verify that they meet the eligibility criteria defined in these Regulations.

b. Prepare a directory of consultants (both individuals and companies) that can assist the DLGs with the basic diagnostic studies and in formulating PRETs.

c. Make recommendations to the Loan Committee for approval of the preinvestment resources needed to carry out the basic diagnostic studies and formulate PRETs.

d. Prepare the terms of reference which the DLGs will use to recruit consultants to carry out basic diagnostic studies and formulate PRETs, and submit these for approval by the Loan Committee.

e. Evaluate the diagnostic studies and PRETs drawn up by the DLGs, and recommend any changes necessary.

f. Prepare draft contracts for subloans and model performance pacts.

g. Negotiate and reach agreement with the DLGs on the performance pacts and subloan contracts.

h. Provide continuous monitoring of compliance with performance pacts and subloan contracts.

i. Design the means by which FIs can record the debts and guarantees issued by DLGs, and provide support for installing this registry within an agency to be designated by the national government.

C. Departmental and local governments (DLGs)

6.4 The duties of the DLGs are to:

a. Apply the resources received under subloans solely for the purposes set out in the PRET, subloan contract and performance pact.

b. Establish a technical operating committee made up of officials from its Finance and Planning Secretariats, with a mandate to monitor compliance with the performance pact and subloan contract, and ensure efficient and effective coordination with the Technical Unit.

c. Facilitate the tasks of the Technical Unit and lenders — including the multilateral lending agencies — in supervising, monitoring and evaluating execution of the subloan.

d. Maintain budgetary and accounting records on the execution of the subloan, employing the detailed breakdown requested by the Central Technical Unit.

e. Provide the guarantees and counterguarantees required by the FIs and the trustee, as the case may be.

f. Have the competent authority certify the grade and amount of its pledge of revenues or levy given in guarantee or counter-guarantee, verifying that this surety meets the minimum percentage requirement set under current legislation.

g. Submit to the Technical Unit a quarterly report on the quantity and quality of activities carried out under the PRET, in accordance with the guidelines specified in the performance pact.

D. FINDETER S.A.

6.5 The duties of FINDETER S.A. are to:

a. Sign performance pacts along with the Ministry of Finance and the DLGs.

b. Administer the trust fund set up by the national government as a means of support for the rediscount lines, assuring FIs that the DLGs will have sufficient resources to meet the obligations under their subloans, and ensuring the commercial viability of operations by guaranteeing debtor liquidity.

c. Sign payment agreements with the DLGs for amounts drawn to service loans with the FIs, charging these to the trust fund.

d. Keep accounting records on the execution of the loans granted by the multilateral lending agencies, and prepare the necessary reports on credit lines.

e. Draft requests for disbursements for submission to the multilateral agencies and justify the application of funds based on eligible expenditures for each lender.

f. Transfer disbursements authorized by the Loan Committee to the FIs under the rediscount mechanism.

E. Financial intermediaries (FIs)

6.6 The duties of the FIs are to:

a. Cooperate with the DLGs in the execution and fulfillment of the performance pacts.

b. Meet all obligations to FINDETER S.A. for access via rediscount to the resources provided under the program.

c. Provide FINDETER S.A. with the information and documentation. required on credit operations financed with program resources.

d. Advise the DLGs on the preparation of applications for subloans.

e. Inform the agency designated by the national government of all debts and pledges of revenues made under credit operations with the DLGs, for purposes of the REG.

F. Submission of requests

6.7 The DLGs will submit applications for access to program resources to the Loan Committee, accompanied by:

a. Letter of intent accepting conditions of the performance pact.

b. Authorization from the departmental assembly or municipal council to sign the subloan contract and performance pact, and to provide the guarantees required by the FIs and trustee.

c. Diagnostic study of the DLG's institutions, financial situation and PRET to ensure that they are consistent with the terms of reference drawn up by the Technical Unit for the program.

G. Evaluation of requests

6.8 The Technical Unit will evaluate applications based on the criteria set out in these Regulations and those established by the Loan Committee, and after which the applications will be submitted to the latter for its approval.

H. Approval of requests

6.9 The Loan Committee will approve subloans.

VII. RECORDS, REPORTS, OVERSIGHT AND MONITORING OF THE PROGRAM

A. Records

7.1 FINDETER S.A. will maintain separate accounting records for each DLG, with breakdown by source of financing and application of funds per component, in accordance with the plan, chart of accounts or coding system indicated by the multilateral lending agencies.

B. Reports

7.2 FINDETER S.A. will submit the reports listed in the respective clauses of approved loan contracts to the funding agencies at regular intervals and according to the deadlines indicated.

C. Oversight and monitoring/audits and inspection

7.3 The multilateral lending agencies financing the program will exercise oversight and monitoring through the reports received each quarter from the Technical Unit. In addition, they will have the option of conducting audits, inspections and in situ evaluations of progress in the activities listed in the PRETs, together with their impact on the financial position and institutions of the DLGs. The agencies may hire specialized consulting services to carry out these tasks.

VIII. ACCELERATED REPAYMENT CLAUSE AND PENALTIES

A. Accelerated repayment clause

8.1 Notwithstanding the amortization period established for subloans, the debt will become immediately payable in full or in part, at the discretion of the Loan Committee, when:

a. One of the events referred to in article 780 of the Commercial Code or article 1533 of the Civil Code, or in the current laws governing debt in Colombia, takes place.

b. A DLG is in arrears on the repayment of the subloan.

c. Resources provided under the program are used for purposes other than the activities listed in the respective PRET.

d. Commitments made in the performance pact are not fulfilled.

e. A DLG interferes with or hinders verification of the application of funds or the status of guarantees.

B. Penalties

8.2 The following penalties are applicable under these Regulations:

a. In accordance with CONPES 2843, FINDETER S.A. will include in its general Credit Regulations provisions requiring as a prerequisite for the approval of new loans under the rediscounting system, that DLGs which have received prior loans under the present program must have complied with the terms and

conditions of the subloan contract and performance pact signed for previous loans.

b. Those penalties established in current legislation on borrowing in Colombia.

c. Any other penalties that the Loan Committee deems appropriate.

IX. OTHER PROVISIONS

A. Entry into force and amendment of these Regulations

9.1 These Regulations shall enter into force on the date when the program is approved by the Loan Committee and the multilateral lending agencies. These parties may suggest amendments and/or the addition of annexes to the present Regulations for the purpose of adapting them to new circumstances or conditions arising in the course of the program, in order that they may remain a means of ensuring the achievement of its objectives. Amendments will enter into effect upon written agreement among the parties.

B. Procurement and disbursement procedures

9.2 Procurement of goods and services, and disbursements under this program shall be subject to the procedures established by the lending agencies financing the program.

C. Accounting and audits

9.3 FINDETER S.A. will maintain separate accounting records of the resources received under loans from each of the agencies financing the program, and these will be audited by an independent firm of public accountants whose selection must be approved by the lending agencies. In addition, these external auditors will state their opinion with respect to the degree to which FINDETER S.A. has complied with the terms and conditions of the loan contracts it has signed. Financial reports on the program requested at intervals by the multilateral lending agencies must be reviewed by the internal auditors employed by FINDETER S.A. before their submission.

D. Inspection and supervision

9.4 The lending agencies will supervise execution of the program through the appropriate units in their headquarters and Country Offices.

E. Interpretation and dispute settlement

9.5 In the event of discrepancies or omissions in these Regulations with respect to the loan contracts signed between the multilateral lending agencies and FINDETER S.A., the latter contracts shall prevail.

PROGRAM REVIEW INDICATORS

	ACTIVITY	ACTIONS		
		1st tranche: disbursement of up to...%	**2nd tranche: disbursement of up to...%**	**3rd tranche: disbursement of up t**
ion	A. Diagnostic study	(i) Diagnostic study: financial and economic situation, indebtedness (budgetary & nonbudgetary), personnel, administrative systems, structures	(i) Diagnostic study updated: reports submitted on financial balances, stock of debt (budgetary & nonbudgetary), personnel and progress of the program.	(i) Diagnostic study updated: repor on financial balances, stock of d (budgetary & nonbudgetary), pe progress of the program.
	B. DLG Economic Reform Plan	(i) DLG Economic Reform Plan drawn up	(i) Satisfactory implementation of the DLG *Economic Reform Plan.*	(i) Satisfactory implementation of th *Economic Reform Plan.*
n of ent rm	C. Requesting, approval and organization of program of reforms	(i) Request to be included in the program, letter of intent to accept conditions, and approval by the departmental Assembly carried out. (ii) Political and technical counterparts designated.		
n of ent rm	D. Immediate actions: Balanced budget	(i) Immediate actions prepared. (ii) Operational savings forecast for the program period. (iii) Forecast stock of debt for the period of the agreement: $... (budgetary & nonbudgetary)	(ii) Forecast operational savings and obtain surplus annualized from previous quarter. (iii) Forecast stock of debt for the period of the agreement (budgetary and nonbudgetary).	(ii) Forecast operational savings and surplus annualized from previou (iii) Nonbudgetary stock of debt redu legal level and budgetary debt r to...% of total expenditures.
n of ent rm	E. Immediate actions: Collection	(i) Taxpayers selected by economic importance. (ii) Inventory of tax debts for collection carried out. (iii) Profile of plan for audit of taxpayers prepared.	(i) Plan for monitoring of selected taxpayers drawn up and approved. (ii) Nonaggressive collection tactics. (iii) Taxpayer audits begun.	(i) Monitoring of at least 50% of the taxpayers. (ii) Legal action to enforce collection (iii) Taxpayer audits being carried ou

	ACTIVITY	ACTIONS		
		1st tranche: disbursement of up to...%	2nd tranche: disbursement of up to...%	3rd tranche: disbursement of up t
of rm	F. *Immediate actions* Administrative reform	*(i) Plan for restructuring of organizations* approved. 1) Elimination of... 2) Merging of... 3) Sale of... (assets) 4) Privatization of... 5, 6..) Other	1) Elimination carried out or necessary legal provision issued 2) Merging carried out or necessary legal provision issued 3) Sale carried out or necessary legal provision *issued* 4) Tenders called for privatization 5, 6..) Other	1) Elimination carried out. 2) Merging operation carried out. 3) Sale carried out. 4) Privatization carried out or firm o *sold.* 5, 6..) Other
	G. Immediate actions Personnel outlays	(i) Begin implementation of the approved employee separation and rationalization plan.	(i) Reduction in total number of positions *forecast in the separation and* rationalization plan, compared to 6-month period before signing of the agreement.	(i) Reduction in total number of pos *forecast in the separation and ra* plan, compared to 6-month perio signing of the agreement.
	H. Institutional strengthening Management of human resources	(i) Diagnostic report on the data and personnel administration system prepared. (ii) Computerized central registry designed. (iii) Personnel census project approved. (iv) Personnel management and standards designed: prevention of absenteeism, checking of licenses, overtime system, etc.	(i) Project for institutional development of the information and personnel *management system approved.* (ii) Central registry on computer with all personnel of the DLG based on existing archives compatible with the approved institutional development program, and updating system implemented. (iii) Census carried out and cross-referencing of data from archives contained in census completed. (iv) Standards implemented.	(i) Project for institutional developm information and personnel mana *system under way.* (ii) Registry in operation and being (iii) Irregularities resolved or legal ac instituted: double dipping, overla schedules, conflicts, etc. (iv) Standards being applied.
	I. Institutional strengthening Tax administration	(i) Plan for institutional development of the tax administration system prepared to the level of...	(i) Plan for institutional development of the tax administration system being implemented.	(i) Plan for institutional developmen administration system implement

ACTIVITY	ACTIONS		
	1st tranche: disbursement of up to...%	2nd tranche: disbursement of up to...%	3rd tranche: disbursement of up
J. Institutional strenghthening Financial administration	(i) Project for institutional development of financial management system (budget, accounting, cash flow, credit) prepared to the level of...	(i) Project for institutional development of financial management system implemented. (ii) Budget or cash commitments performance implemented.	(i) Project for institutional developme financial management system imp (ii) Budget or cash commitments perf implemented (iii) Stock of nonbudgetary debt reduc limit and budgetary debt to __% o expenditure

LOGICAL FRAMEWORK
INSTITUTIONAL STRENGTHENING OF DEPARTMENTAL AND LOCAL GOVERNMENTS (CO-0155)

OBJECTIVES	INDICATORS	MEANS OF VERIFICATION	ASSUMPTIONS
lidation of the decentralization ombia	– Efficiency and effectiveness in the provision of services by the local governments. – Increase in public participation in decision making. – Results when management of central government institutions take a leading role in the reform process.	– Consulting with the public concerning the quality of services. – Consulting with the public concerning the practicality and responsiveness of mechanisms for public participation. – Evaluating the effectiveness of efforts by central government institutions involved in the decentralization process.	– The decentralization process co receive political support at the l – The process continues to receiv support from the central govern
overnments on a sound financial	– *Sustainability of public finances in the DLGs.*	– Reviewing the economic and institutional organization of regional entities.	– The program continues to recei support at the local and nationa – Adoption of a DLG Government Reform Plan.
sustainability of reforms by nstitutional strengthening for the nments.	– Modern institutions for tax and financial administration.	– Checking the indicators of tax and financial administration. – Checking that processes are integrated.	– Adoption of reform measures to technical capacity of DLGs.
adership and management the central government in the rgovernmental fiscal relations.	– Improved results by management of central government agencies. – Improvement in the quality and availability of information at the regional level.	– Reviewing the management of the Fiscal Support Division. – Examining the results from the Registry of Debt and Guarantees.	– The government maintains its c to strengthening its institutions.
COMPONENTS ion of public finances: economic measures to generate savings by increasing revenues *ng inefficient expenditures.*	– Indicators of a balanced budget: positive operational savings for more than five consecutive quarters and debt-to-current revenues ratio stable and less than 80%.	– Reviewing fiscal indicators of revenues, expenditures and debt each quarter.	– The financial intermediaries gra under the program. – The reforms adopted are sustai continuous.

OBJECTIVES	INDICATORS	MEANS OF VERIFICATION	ASSUMPTIONS
strengthening in DLGs:			
entation of modern systems of inistration.	– Quarterly results for tax revenues.	– Checking development of DLG tax revenues each quarter.	
entation of modern systems of l administration.	– Quarterly results for expenditures and indebtedness.	– Checking development of DLG expenditures and indebtedness each quarter.	
ement of human resources.	– Efficiency of managerial staff in DLG.	– Reviewing the qualifications of employees with senior duties in the DLGs.	
strengthening for central t:			
chnology support and human n the Fiscal Support Division cilitate monitoring of regional	– Number of officials hired and modern information systems installed in the DAF.	– Reviewing the qualifications of employees with senior duties within the DLGs.	
ACTIVITIES			
on of public finances:			
ture the DLGs	– Studies completed on the organizational structure and the possible transfer of assets.	– Reviewing final versions of documents.	– That the program receives politi
the operations and business s of DLGs			– That DLG leadership is forthcon
funding for severance pay, enefits and back-pay owed to nel affected by downsizing.	– Number of employees leaving the civil service and positions canceled.	– Review records of employees terminated along with their severance pay and benefits.	– That no serious resistance to ch develops among key personnel sector.
strengthening in regions:			
ninistration: update the Income de; prepare and update ational manuals and job tions; replace the current system ed around specific taxes with a inistration based on functions; and put in place audit programs d to broaden the tax base.	– Income tax codes and organizational manuals updated; tax administration system based on functions operational; taxpayer list updated.	– Visiting DLGs and examining their tax administration systems. – Reviewing income tax codes, organizational manuals and taxpayer lists of DLGs.	– That the changes are executed manner.

OBJECTIVES	INDICATORS	MEANS OF VERIFICATION	ASSUMPTIONS
al administration: develop and ent an integrated financial ement system; improve the and evaluation of the budget; te borrowing procedures; adjust s to standards established by the roller General's Office.	- Budget process integrated, including treasury, budget, credit and accounting components.	- Visiting regional entities and examining their financial administration systems.	
resources: strengthen ement of human resources, nizing employment regulations ta system.	- Budget standardized for central administration and decentralized agencies of DLGs.	- Reviewing the budget. - Reviewing the financial statements.	
l strengthening for central nt:			
hen the role of the DAF in the ring of fiscal matters, using ized consultants.	- Professional assistance and technology for the DAF.	- Reviewing qualifications of DAF advisers.	
an REG to improve the quality of nancial data and thus facilitate ring by the DAF.	- Operational efficiency of the REG.	- Plan with data on debt and guarantees of governments receiving loans and, after two years, on eligible DLGs.	

TENTATIVE PROCUREMENT SCHEDULE
(US$)

MAIN ITEMS OF PROCUREMENT 1/	TOTAL	FINANCING IDB	CAF	LOCAL	METHOD	PREQUALIFICATION	DATE OF SPN Period / Year
I. **CONSULTING SERVICES 2/** (Individual consultants only. *Maximum monthly cost per consultant = US$8,000)*							
1. Fiscal reform							
1.1 Studies	200,000	60%	40%		CP	ROC	I /97
	150,000	60%	40%		CP	ROC	II /97
	150,000	60%	40%		CP	ROC	I /98
1.2 Preparation of PRETs	559,680			100%	CP	ROC	I /97
	419,760			100%	CP	ROC	II /97
	419,760			100%	CP	ROC	I /98
2. Institutional Strengthening							
2.1 Program coordination (Central Technical Unit)							
a. Coordination of the Central Technical Unit	400,000			100%	CP	ROC	I /97
b. Material support (coordination of activities in tax and financial administration, human resources management, information systems, rationalization of structures and separation component).	2,525,000			100%	CP	ROC	I /97
c. Technical support (legal assistance, assistance with contract process).	1,085,000			100%	CP	ROC	I /97
d. Administrative support (administrative and financial coordination, contracts, and logistics)	990,000			100%	CP	ROC	I /97
2.2 Tax and Financial administration systems							
a. Coordination (10 DLG technical units)	1,584,000	63%	37%		CP	ROC	I /97
	1,188,000	63%	37%		CP	ROC	II /97
	1,188,000	63%	37%		CP	ROC	I /98
b. Development of tax administration systems							
b.1 Development of taxpayer master file	401,538	64%	36%		CP	ROC	I /97
	301,154	64%	36%		CP	ROC	II /97
	301,154	64%	36%		CP	ROC	I /98
b.2 Revenue collection systems (current account)	902,000	64%	36%		CP	ROC	II /97
	676,500	64%	36%		CP	ROC	I /98
	676,500	64%	36%		CP	ROC	II / 98
b.3 Auditing systems	356,923	64%	36%		CP	ROC	I /98
	267,692	64%	36%		CP	ROC	II / 98
	267,692	64%	36%		CP	ROC	I / 99
c. Development of financial administration systems							
c.1 . Budgeting systems	902,000	64%	36%		CP	ROC	I /97
	676,500	64%	36%		CP	ROC	II /97
	676,500	64%	36%		CP	ROC	I /98
c.2 . Treasury systems	484,600	64%	36%		CP	ROC	II /97
	363,450	64%	36%		CP	ROC	I /98
	363,450	64%	36%		CP	ROC	II / 98
c.3 Accounting systems	484,600	64%	36%		CP	ROC	II /97
	363,450	64%	36%		CP	ROC	I /98
	363,450	64%	36%		CP	ROC	II / 98
c.4 Public borrowing systems	276,750	64%	36%		CP	ROC	II /97
	276,750	64%	36%		CP	ROC	I /98
	184,500	64%	36%		CP	ROC	II / 98
	184,500	64%	36%		CP	ROC	I /99
e. Information systems plan	792,000	64%	36%		CP	ROC	I /97
	594,000	64%	36%		CP	ROC	II /97
	594,000	64%	36%		CP	ROC	I /98

TENTATIVE PROCUREMENT SCHEDULE
(US$)

MAIN ITEMS OF PROCUREMENT 1/	TOTAL	FINANCING IDB	CAF	LOCAL	METHOD	PREQUALIFICATION	DATE OF SPN Period / Year
I. **CONSULTING SERVICES** (Cont.) 2/							
2.3. Establishment of Registry of Debt and Guarantees	600,000			100%	CP	ROC	I /97
2.4. Human resources / staff training	270,000	59%	41%		CP	ROC	II /97
	270,000	59%	41%		CP	ROC	I /98
	270,000	59%	41%		CP	ROC	II / 98
	270,000	59%	41%		CP	ROC	I /99
	270,000	59%	41%		CP	ROC	II / 99
II. **EQUIPMENT**							
1. Computer equipment and programs	431,200	64%	36%		LB	YES	I /97
Various packages	671,800	64%	36%		LB	YES	II /97
(Purchasing will not be centralized and all bidding will be	560,500	64%	36%		LB	YES	I /98
for contracts of less than US$100,000)	292,900	64%	36%		LB	YES	II / 98
	205,445	64%	36%		LB	YES	I /99
2. Training supplies / office equipment / communications	143,830	64%	36%		LB	YES	I /97
Various packages	193,300	64%	36%		LB	YES	II /97
(Purchasing will not be centralized and all bidding will be	163,700	64%	36%		LB	YES	I /98
for contracts of less than US$100,000)	79,885	64%	36%		LB	YES	II / 98
	59,400	64%	36%		LB	YES	I /99

1/ Amounts are based on estimates for participation by 10 DLGs. It is assumed that 4 DLGs will join the program and initiate institutional strengthening activities in the first half of 1997, another 3 will do so in the second half of 1997, and 3 more in the first half of 1998.
2/ Consulting firms will not be hired. All contracts will be with individual consultants.

Note

CP = Calls for proposals
LB = Local competitive bidding not restricted to international firms
ROC = Registry of Consultants

LEGIII/CO-7189

PROPOSED RESOLUTION

COLOMBIA. ___/OC-CO TO THE FINANCIERA DE DESARROLLO TERRITORIAL S.A.
TERRITORIAL ENTITY STRENGTHENING PROGRAM (CO-0155)

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf the Bank, to enter into such contract or contracts as may be necessary with the Financiera de Desarrollo Territorial, S.A., as Borrower, and the Republic of Colombia, as Guarantor, for the purpose of granting the former a financing to cooperate in a territorial entity strengthening program. Such financing will be for the amount of up to Forty Million United States of America dollars (US$40,000,000), from the Single Currency Facility of the Ordinary Capital resources of the Bank, and will be subject to the "Terms and Financial Conditions" and "Special Contractual Conditions" of the Executive Summary of the Loan Proposal.