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BRAZIL

FISCAL MANAGEMENT MODERNIZATION PROGRAM FOR THE STATE OF PARAÍBA (PROFISCO II – PB)

(BR-L1535)

THIRTEENTH INDIVIDUAL LOAN OPERATION UNDER THE CONDITIONAL CREDIT LINE FOR INVESTMENT PROJECTS (CCLIP) FISCAL MANAGEMENT MODERNIZATION PROGRAM IN BRAZIL – PROFISCO II

(BR-X1039)

LOAN PROPOSAL

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ABBREVIATIONS

CAPAG	Metodologia de Avaliação da Capacidade de Pagamento [Payment Capacity Assessment Methodology]
CCLIP	Conditional credit line for investment projects
CGE/PB	Controladoria Geral do Estado do Paraíba [Office of the State Comptroller General]
CIAT	Inter-American Center of Tax Administrations
COGEF	Comissão de Gestão Fazendária [Treasury Management Commission]
CONFAZ	Conselho Nacional de Política Fazendária [National Council for Tax Policy]
GOA	Gerência Operacional de Acompanhamento [Operations Monitoring Unit]
IBGE	Instituto Brasileiro de Geografia e Estatística [Brazilian Institute of Geography and Statistics]
ICMS	Imposto sobre circulação de mercadorias e prestação de serviços [goods and services sales tax]
ICT	Information and communications technology
IPM	Índice de participação municipal [municipal revenue-sharing index]
IT	Information technology
LDO	Lei de Diretrizes Orçamentárias [Budget Guidelines Law]
LOA	Lei do Orçamento Anual [Annual Budget Law]
MD-GEFIS	Avaliação da Maturidade e Desempenho da Gestão Fiscal [Fiscal Management Maturity and Performance Assessment]
MTBF	Medium-term budgetary framework
NCB	National competitive bidding
NCI	Net current income
NF-e	Nota fiscal eletrônica [electronic tax invoice]
PCR	Project completion report
PCU	Project coordination unit
PGE/PB	Procuradoria-Geral do Estado [Office of the State Attorney General]
PGFN	Procuradoria-Geral da Fazenda Nacional [Office of the General Counsel to the National Treasury]
PNAFM	Programa Nacional de Apoio à Gestão Administrativa e Fiscal dos Municípios Brasileiros [National Program to Support the Administrative and Fiscal Management of Brazilian Municípios]
PPA	Plano Plurianual [Multiyear Plan]
PROFISCO	Programa de Apoio à Gestão e Integração dos Fiscos no Brasil [Program to Support the Management and Integration of Tax Administrations in Brazil]
QCBS	Quality- and cost-based selection
REDESIM	Rede Nacional para a Simplificação do Registo e da Legalização de Empresas e Negócios [National Network for Simplified Registration and Legalization of Businesses and Firms]
SBC	Special Bidding Committee
SEAD	Secretaria de Estado de Administração [Administration Department]
SEFAZ/PB	Secretaria de Fazenda do Estado do Paraíba [State of Paraíba Finance Department]

SEPLAG	Secretaria de Estado de Planejamento e Gestão [Planning, Budget, and Management Department]
SIAF	Sistema Integrado de Administração Financeira [Integrated Financial Administration System]
SICgov	Sistema de Informações de Custo do Governo Federal [Federal Government Cost Information System]
SICONFI	Sistema de Informações Contábeis e Fiscais do Setor Público Brasileiro [Brazilian Public Sector Accounting and Fiscal Information System]
SIOP	Sistema Integrado de Planejamento e Orçamento [Integrated Planning and Budget System]
SOE	State-owned enterprise
SPED	Sistema Público de Escrituração Digital [Digital Public Accounting System]
SRF	Secretaria da Receita Federal [Federal Revenue Service]
STN	Secretaria do Tesouro Nacional [National Treasury Department]
TCE/PB	Tribunal de Contas do Estado do Paraíba [State of Paraíba Audit Office]

PROJECT SUMMARY

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(PROFISCO II – PB)
(BR-L1535)

THIRTEENTH INDIVIDUAL LOAN OPERATION UNDER THE CONDITIONAL CREDIT LINE FOR INVESTMENT PROJECTS (CCLIP) FISCAL MANAGEMENT MODERNIZATION PROGRAM IN BRAZIL – PROFISCO II (BR-X1039)

Financial Terms and Conditions				
Borrower:			**Flexible Financing Facility**[a]	
State of Paraíba (PB)			**Amortization period:**	25 years
Guarantor:				
Federative Republic of Brazil			**Disbursement period:**	5 years
Executing agency:				
State of Paraíba, acting through its Finance Department (SEFAZ/PB)			**Grace period:**	5.5 years[b]
Source	**Amount (US$)**	**%**	**Interest rate:**	LIBOR-based
IDB (Ordinary Capital):	38,412,000	90%	**Credit fee:**	[c]
			Inspection and supervision fee:	[c]
Local:	4,268,000	10%	**Weighted average life:**	15.25 years
Total:	42,680,000	100%	**Currency of approval:**	U.S. dollars

Project at a Glance
Project objective/description: The project objective is to contribute to the fiscal sustainability of the State of Paraíba through the following specific objectives: (i) modernization of fiscal management; (ii) improvement of tax administration, and (iii) improvement of public expenditure management. This project is the thirteenth individual loan operation under the PROFISCO II CCLIP (BR-X1039), approved by the Board of Executive Directors pursuant to Resolution DE-113/17.
Special contractual conditions precedent to the first disbursement of the loan proceeds: (i) the borrower will adhere to the program Operating Regulations previously approved by the Bank for all individual operations under the PROFISCO II CCLIP; and (ii) the project coordination unit has been established, and its members appointed (see paragraph 3.4). **Special contractual conditions for execution:** Prior to the start of execution of activities with outputs intended for the Planning, Budget, and Management Department (SEPLAG), the Administration Department (SEAD), the Office of the State Comptroller General (CGE/PB), and the Office of the State Attorney General (PGE/PB), SEFAZ/PB will sign a legal instrument with those entities of the borrower, to establish the roles and responsibilities of the parties during execution of the respective activities (see paragraph 3.5).
Exceptions to Bank policies: None.

Strategic Alignment						
Challenges:[d]	SI	☐	PI	☑	EI	☐
Crosscutting themes:[e]	GD	☐	CC	☑	IC	☑

[a] Under the terms of the Flexible Financing Facility (document FN-655-1), the borrower has the option of requesting changes to the amortization schedule as well as currency, interest rate, and commodity conversions. The Bank will take operational and risk management considerations into account when reviewing such requests.

[b] Under the flexible repayment options of the Flexible Financing Facility, changes to the grace period are permitted provided that they do not entail any extension of the original weighted average life of the loan or the last payment date as documented in the loan contract.

[c] The credit fee and inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with the applicable policies.

[d] SI (Social Inclusion and Equality); PI (Productivity and Innovation); and EI (Economic Integration).

[e] GD (Gender Equality and Diversity); CC (Climate Change and Environmental Sustainability); and IC (Institutional Capacity and Rule of Law).

I. DESCRIPTION AND RESULTS MONITORING

A. Background, problem to be addressed, and rationale

1.1 This project is the thirteenth individual loan operation under the conditional credit line for investment projects (CCLIP) for the Fiscal Management Modernization Program in Brazil (PROFISCO II) (BR-X1039), approved by the Bank's Board of Executive Directors pursuant to Resolution DE-113/17, to consolidate the progress made by the PROFISCO I CCLIP (BR-X1005) and continue the modernize the fiscal management of the states.

1.2 The PROFISCO II CCLIP (BR-X1039) was approved in 2017 for US$900 million with the objective of contributing to fiscal sustainability through the following specific objectives: (i) the modernization of fiscal management; (ii) upgrading of the tax administration; and (iii) better public expenditure management. Agencies of Brazil's 26 states, the Federal District, and the Federative Republic of Brazil that receive a favorable recommendation from the Ministry of Planning's External Financing Commission are eligible as borrowers for the preparation of an individual operation.[1]

1.3 The PROFISCO II CCLIP seeks to increase revenue intake and improve the country's business environment and competitiveness, and was primarily designed to support: (i) enhancement of the functionality of the Digital Public Accounting System (SPED) in tax audit automation and tax obligations; (ii) improvement of public expenditure quality in the adoption of multiyear budgeting and introduction of public procurement and public investment systems; (iii) introduction of new technologies such as big data for the audit and management of public expenditures, cybersecurity for data security, and the use of bots for taxpayer service interactions; and (iv) strengthening of the processes, methodologies, and technologies already supported by the PROFISCO I CCLIP.

1.4 **In the past five years, Brazil has been facing major challenges in keeping its economy growing at a sustainable pace.** National GDP shrank 3.2% in 2015, and 3.3% in 2016. It rallied somewhat in 2017-2018, growing 1.3% each year,[2] but growth was 1.1% in 2019, when the central government posted a primary deficit of 1.22% of GDP, down from 1.69% in 2018; in December 2019, the gross public debt was 75.8% of GDP, down 0.8% from January of that year. The government sent three constitutional amendments to Congress in 2019, to address fiscal emergencies, fiscal federalism, and rationalization of public funds. In addition, the government and Congress are preparing reforms to the tax system and the public administration that are fundamental for improving the efficiency and sustainability of fiscal policy.

1.5 **The COVID-19 pandemic and the health crisis**. The health crisis battered the economy in 2020 and expectations for economic activity, affecting domestic demand and supply. The central bank's FOCUS[3] report indicates that growth expectations for 2020 have fallen to -4.66%, well below the 2.30% forecast at the start of the year. Expectations are for growth in the next three years of 3.31% in 2021 and 2.5% in

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1 Thus far, the Bank's Board of Executive Directors has approved 12 projects (Ceará, Piauí, Pará, Maranhão, Pernambuco, Mato Grosso do Sul, São Paulo, Espírito Santo, Amapá, Paraná, Bahia and Rio Grande do Sul) totaling US$574.65 million.

2 Brazilian Institute of Geography and Statistics (IBGE), 2018.

3 Focus Report.

2022 and 2023. To mitigate the negative impact of the turmoil, Congress approved a state of civil emergency due to the COVID-19 pandemic, enabling the federal government to diverge from the fiscal target set for 2020. Other measures include income and employment support programs, strengthening of the health budget, social transfers, financial assistance to subnational entities, financial support to small and medium-sized enterprises (SMEs), import tariff reductions, and tax deferrals, and others. The total fiscal impact of the measures announced thus far amounts to almost 300 billion Brazilian reais, or 3.8% of national GDP. Projected primary deficits as a percentage of national GDP are 12% in 2020, 3% in 2021, 2.01% in 2022, and 1.5% in 2023

1.6 **Fiscal position of Paraíba (PB).** In 2019, the state of Paraíba had about 4 million inhabitants, accounting for 1.9% of Brazil's total population. The state's GDP represented 0.9% of the national total, ranking it the nineteenth largest economy among the 27 Brazilian states.[4] Despite the state's financial balance, its fiscal sustainability is at risk. Net current income (NCI) rose 6.9% in real terms between 2012 and 2018, while tax revenues increased by 17.4%. This result was heavily influenced by the revenue performance of the goods and services sales tax (ICMS), which generated 52.7% of NCI in 2012, rising to 57% in 2018. Net current expenditure grew more slowly than NCI, increasing just 4.4% between 2012-2018, in response to payroll containment measures.[5] Nonetheless, government payroll expenditures still absorbed 50.6% of NCI in 2018, which was close to the limit set by the Fiscal Responsibility Law (LRF), and pension-related expenditures continue to rise. In recent years, investment has represented about 1% of the state's GDP, which is very low for its level of social[6] and economic development. The consolidated debt is relatively low and has been trending down (from 51.3% of NCI in 2012 to 48% in 2018). See State of Paraíba fiscal analysis.

1.7 The economic and health situation during 2020 will impact Paraíba's public finances. The pandemic led to the shutdown of nonessential activities for a few weeks and to social distancing measures, which are expected to affect economic activity and tax revenue. During the period from January to August 2020, tax revenue was down 2.89% compared to the same period in 2019, versus a reduction of 3.0% for all states as a whole.[7] The state of Paraíba, for its part, has expanded public spending for services to the population,[8] but an important part has been financed with transfers from the federal government, so the impact on the public accounts is expected to be limited.

1.8 **Rationale.** The state's fiscal vulnerability, resulting from high payroll expenditures and the need for greater investment associated the fiscal risk posed by the COVID-19 pandemic crisis, highlight the urgent need for new fiscal management modernization actions, to achieve fiscal sustainability. In addition, new, complementary approaches are necessary to bolster the state's fiscal performance.

[4] IBGE. 2016 is the last year with statistics available for all Brazilian states.

[5] The state suspended staff merit increases, raising wages only by the legal obligation to keep pace with inflation.

[6] Atlas of Human Development in Brazil: Paraíba's Human Development Index (HDI) was 0.656 in 2018.

[7] National Council for Tax Policy, CONFAZ, 2020.

[8] COVID-19 data from Paraíba.

The PROFISCO I – PB operation put great emphasis on improving tax administration and fostered integration of the state tax authorities with other levels of government by implementing the Digital Public Accounting System (SPED) and the electronic tax invoice (NF-e). These efforts enabled Paraíba to partly counteract the effects of the 2015-2016 economic crisis, chiefly by maintaining its internally generated revenue and facilitating tax compliance, which, in conjunction with the fiscal adjustment measures, have contributed to maintaining a "B" rating, to date (November 2020), in the "ability to pay" (CAPAG) methodology of the National Treasury Department (STN) (see paragraph 2.7). This project will continue to modernize revenue collection and will further develop the public expenditure issues by promoting: (i) the strengthening of financial administration; (ii) the strengthening of public expenditure management and quality; (iii) the use of digital technologies; and (iv) the simplification of tax compliance to improve the business environment.

1.9 The effectiveness and efficiency of public institutions are constrained by the restrictions faced by their staff, access to information technologies, the availability of financial resources, and the legal framework (Arenas de Mesa, 2016; Finan et al., 2017). The government therefore needs to address remaining weaknesses that hamper its fiscal performance. In terms of human resources, the State of Paraíba Finance Department (SEFAZ/PB) has a payroll of approximately 658.[9] However, it has no methodologies or procedures for evaluating and sizing its workforce that would enable it to quantify and determine the qualifications and composition of its personnel, so the staff allocation does not address the institution's current and future needs or enable better targeting of skills-based training.

1.10 In terms of technology constraints, the SEFAZ/PB information technology (IT) infrastructure is stretched to the limit in processing and storage capacity.[10] The computer, telecommunications, and security infrastructure is projected be insufficient in 2020. With the recent entry into operation of the electronic invoice, in the next five years it will be necessary to expand storage capacity from 250 to 500 terabytes and raise processing capacity from 2,074 to 3,111 GHz. The market availability of state-of-the-art technology opens a window for sustainable, safe, and efficient expansion of technology, even in terms of energy consumption, which will contribute to lower costs and prevent greenhouse gas emissions.

1.11 Lastly, in terms of the legal framework,[11] although the state of Paraíba has a Tax Code consolidated into a single law, it has difficulty consolidating tax legislation and keeping it up to date. It also finds it difficult to respond to internal and external queries in a user-friendly manner, which undermines legal certainty in the enforcement of tax law.

1.12 Compounding these factors, climate change and natural disasters can also affect fiscal management by causing economic losses and imposing an additional burden on development and poverty-reduction policies. The fiscal impacts of natural disasters arise from the need for unplanned expenditures and the loss of revenue

[9] Technical note – Personnel management.

[10] Technical note – Information technology.

[11] Technical note – Tax policy.

following the disruption of economic activities and the consequent shrinkage of the tax base[12] (see Climate change document).

1.13 In view of all this, Paraíba has requested the Bank's support to mitigate the three main specific problems deterring the state from achieving fiscal balance, as outlined below:[13]

1.14 **In fiscal management and transparency**, SEFAZ/PB's corporate processes in the areas of governance and strategic management, as well as management of personnel, technology, and communication with citizens are insufficiently developed and integrated, which limits its institutional performance. This is a consequence of the following:

a. **The state's strategic management has weaknesses in planning, evaluation of institutional performance, and risk management**,[14] owing to: (i) insufficient integration and vaguely defined roles and responsibilities of the fiscal management entities; (ii) difficulty in identifying, measuring, and mitigating the risks jeopardizing the achievement of strategic and operational objectives; (iii) the fact that the outcomes of government programs and projects are not evaluated and do not provide adequate feedback; (iv) low level of maturity of the government's internal audit, due to the lack of a quality program for procedures; (v) difficulty in assessing and sanctioning the ethical conduct of state civil servants, due to weaknesses in existing procedures; and (vi) insufficient control of compliance with existing rules in the execution of administrative and operational procedures.

b. **The state's labor force is not making the most of its human resource skills, diminishing the quality of service delivery**,[15] owing to: (i) no standardized model of personnel management for the fiscal management institutions: SEFAZ/PB, the Planning, Budget, and Management Department (SEPLAG), the Office of the State Attorney General (PGE/PB), the Office of the State Comptroller General (CGE/PB), and the Administration Department (SEAD); (ii) weak culture of knowledge dissemination among government entities; and (iii) staff training that does not consider the skills profile of civil servants relative to their duties.

c. **SEFAZ/PB's information technology infrastructure used to manage tax data has major weaknesses**,[16] owing to: (i) no governance of information and communication technology (ICT) services, which impacts services and fails to address several different areas of tax management in the performance of activities; (ii) out-of-date ICT hardware relative to the new technologies and tools; (iii) no standardization of ICT service requests, resulting in low responsiveness; (iv) out-of-date software and hardware infrastructure, including hardware at the end of its useful life, which impacts energy

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12 OECD/World Bank (2019). Fiscal Resilience to Natural Disasters: Lessons from Country Experiences, OECD Publishing.

13 The diagnostic assessment looked at fiscal management maturity as measured using the MD-GEFIS Fiscal Management Maturity and Performance methodology.

14 Technical note – Strategic management.

15 Technical note – Personnel management.

16 Technical note – IT.

consumption; (v) corporate systems that do not serve users satisfactorily or generate timely information for decision-making; (vi) information security and physical access tools that fall short in protecting taxpayer data; and (vii) insufficient data processing and storage capacity to handle a large volume of new electronic tax documents.

d. **State procurement management shows weaknesses in the processes conducted by management units**,[17] owing to: (i) insufficient planning to execute procurements (the purchasing center is not proactive and only responds to agency demand); and (ii) an obsolete procurement system that does not issue management reports and is not integrated with other government systems.

e. **Little participation by society in fiscal transparency and citizenship programs**,[18] owing to: (i) the fragility of societal oversight instruments and transparency of government actions and mechanisms for user participation in public services; (ii) the diversity and lack of integration of protocol systems (information, requests, and complaints) within state agencies; and (iii) a missing or weak strategic vision of the government's fiscal education program, making it less prominent in the minds of civil servants and society.

1.15 **In tax administration and tax litigation**, revenue performance falls short of potential,[19] as a consequence of the following:

a. **Inefficiency and weak control of tax policy support instruments**,[20] owing to difficulties in: (i) formulating and reviewing priority tax policies; (ii) estimating the impact of tax concessions granted; (iii) estimating tax evasion; and (iv) consolidating and keeping tax legislation up to date, as well as responding to internal and external queries in a user-friendly manner.

b. **Insufficient management and control of the state's economic and fiscal data**,[21] owing to: (i) delays in completing the taxpayer registration process, due to the large number of processes generated by the National Network for Simplified Registration and Legalization of Businesses and Firms (REDESIM); (ii) difficulty in paying foreign trade taxes; (iii) difficulty in calculating the municipal revenue sharing index (IPM) for the state goods and services sales tax (ICMS); (iv) the large number of ancillary tax obligations; and (v) difficulty in tracking delinquent taxpayers under the "Simples Nacional" simplified tax regime.

c. **Difficulty in supervising taxpayers on a mass scale**,[22] owing to: (i) inability to identify irregularities in the shipment of goods and supervise them physically; (ii) isolated and nonstandardized operation of the different fiscal controls

[17] Technical note – Procurement management.

[18] Technical note – Fiscal transparency.

[19] Although the PROFISCO I – PB project contributed to increasing the state's tax revenue intake, Paraíba's ICMS-to-NCI ratio of 41.9% is still below the 50.84% average for Brazilian states.

[20] Technical note – Tax policy.

[21] Technical note – Economic and fiscal information.

[22] Technical note – Audit.

instruments (networks); and (iii) difficulty in identifying structured and complex fraud.

d. **Inefficiency in the management of tax litigation and low efficiency in the recovery of adjudicated tax debts**,[23] owing to: (i) slow decision-making in tax cases; (ii) insufficient integration of SEFAZ/PB and PGE/PB tax administration procedures and systems; and (iii) high transaction costs in enforced collection, since nearly all cases go to trial.

e. **Insufficient support for taxpayers to meet their tax obligations**,[24] owing to the following: (i) the large number of taxpayer services provided in person; (ii) not all available services use the taxpayer's electronic address; and (iii) the infrastructure for face-to-face interaction is inadequate, and the services provided are not evaluated for quality.

f. **Difficulty in actually collecting tax**,[25] owing to the difficulty in identifying the most recoverable claims and identifying the taxpayer's risk profile, as well as no preset rules for financing the payment of taxes owed.

1.16 **In public expenditure management**, shortcomings make it difficult to improve results in terms of fiscal discipline and public expenditure efficiency and effectiveness.[26] The causes are:

a. **Insufficient capacity for planning and evaluating the effectiveness of public policies implemented by the government**,[27] owing to: (i) difficulty in globally monitoring government programs, projects, and actions because the information is not integrated; and (ii) insufficient knowledge of public policy management issues by the personnel involved in the process.

b. **Inefficiency in management unit planning of financial execution with expenditures above the authorized ceilings**,[28] owing to difficulties in: (i) collecting, estimating, and monitoring information for government cash management; and (ii) controlling the expenditure ceilings for management unit financial execution.

c. **Difficulty in supervising administrative and financial management in state-owned enterprises**,[29] owing to: (i) noncompliance with the law on state-owned enterprises (SOEs), leading to wasted resources for the state government; (ii) decision-making difficulties due to a failure to monitor the performance of SOEs; and (iii) insufficient knowledge of SOE management issues by the human resources involved in the process.

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23 Technical note – Tax litigation.

24 Technical note – Taxpayer services.

25 Technical note – Revenue and collection.

26 Better Spending for Better Lives, IDB. Infrastructure cost overruns and delays in Latin America and the Caribbean are estimated to represent 0.7% of GDP, and waste in public procurement is estimated at between 0.9% and 2.6% of GDP.

27 Technical note – Monitoring of government actions.

28 Technical note – Financial management.

29 Technical note – Management of state-owned enterprises. There are currently 13 SOEs with a total budget of approximately 1,032,278,626 reais that are not adequately supervised for compliance with their governing law.

d. **Insufficient consolidated accounting data to support the decision-making process**,[30] owing to: (i) important unmet requirements for completing the accounting convergence process, mainly concerning adjustments to the corresponding information technology systems and data security; (ii) limited knowledge of information on the state's real estate assets; and (iii) unknown unit costs of public services provided to society.

e. **Difficulty in tracking the indebtedness of the state's public enterprises, in terms of both actual and contingent liabilities**,[31] owing to: (i) unknown risks of liabilities that could compromise the state's public debt; and (ii) debt management system that lacks the required functionalities to operate and has difficulties in exchanging data with the financial system.

f. **Inefficient management of state public investment**,[32] owing to: (i) the absence of structured processes for public investment management; (ii) difficulties in prioritizing the main state investments, due to the lack of methodologies and tools to integrate socioeconomic and climate change vulnerability indicators when calculating investment gaps;[33] (iii) the absence of systematized procedures for the preparation and ex ante evaluation of investment projects; (iv) delays in the execution of investment projects; and (v) the absence of procedures for monitoring the implementation of investment projects.

1.17 **The Bank's experience in the country.** The Bank has supported fiscal management modernization at the three levels of government in Brazil, achieving significant transformations over the more than 25 years of programs implemented, especially at the state level under the National Fiscal Administration Program for the Brazilian States (PNAFE) (980/OC-BR), the PROFISCO I CCLIP (BR-X1005), and the Fiscal Stability Consolidation Programs for Development (PROCONFIS).[34] These projects supported implementation of the electronic tax invoice (NF-e), which enables firms to submit their tax and accounting data to the tax authorities via digital media, and the Integrated Financial Administration Systems (SIAFs) compatible with international accounting standards. It also strengthened technological capacity for the storage and processing of electronic tax data, as well as the public procurement system. The main outcomes were increased tax revenue intake, decreased informality, and lower transaction costs for the tax authorities and taxpayers.[35] According to the midterm evaluation of the PROFISCO I CCLIP,[36] between 2009 and 2013, states with a PROFISCO project at an advanced stage were taking in an average of 6% more in ICMS revenue than states with a PROFISCO project in its early stages. For the municípios, the National Program to Support the Administrative

30 Technical note – Accounting management.

31 Technical note – Public debt management.

32 Technical note – Public investment management.

33 The climate change document contextualizes the state's vulnerability to climate change and its effects on fiscal management.

34 Policy-based loan programs: 2081/OC-BR, 2841/OC-BR, 2850/OC-BR, 3039/OC-BR, 3061/OC-BR, 3138/OC-BR, and 3139/OC-BR.

35 Midterm evaluation and PROFISCO I – PB project completion report (PCR).

36 Midterm evaluation and PROFISCO I – PB PCR.

and Fiscal Management of Brazilian Municípios (PNAFM),[37] now in its third phase, supports the growth of internally generated revenue by implementing the electronic invoice for services, updating the real estate cadastre, decreasing administrative costs, and increasing taxpayer services. At the federal level, with the Federal Revenue Service Fiscal Modernization Program[38] and the Finance Ministry Integrated Modernization Program (PROFISCO/PMIMF),[39] the Bank supported implementation of the risk management and antifraud intelligence methodology at the Office of the General Counsel to the Treasury, the Brazilian Public Sector Accounting and Fiscal Information System (SICONFI), and the Federal Government Cost Information System (SICgov), among other actions.

1.18 In relation to PROFISCO I – PB (loan 2184/OC-BR),[40] which was executed in the original five-year period, the final evaluation concluded that the project had performed successfully (Relevance – Excellent; Effectiveness – Satisfactory; Efficiency – Excellent; and Sustainability – Excellent). Of the 16 planned outcome targets, 12 (75%) were fully met, and the other 4 (25%) were partially met. The project had 21 output targets, 20 (95.24%) of which were fully met. In relation to tax revenues, SPED, which includes the NF-e, was the action that most directly contributed to the increase in the state's tax revenue intake. In relation to public expenditure, the SIAF contributed to more effective financial management, promoting greater accountability and enhanced transparency, as well as increased integration of the information generated by the state's various public finance systems (budget, treasury, accounting, and debt). The performance of the executing agency and the Bank were rated satisfactory. The team that executed PROFISCO I – PB is also expected to execute PROFISCO II – PB.

1.19 **Lessons learned from the Bank's operations in the country.** The lessons learned from PROFISCO I CCLIP[41] and PROFISCO I – PB include the following:

a. **Design.** The need for an instrument to identify innovative solutions in fiscal management processes. That was the reason for developing the Fiscal Management Maturity and Performance Assessment (MD-GEFIS), which identifies the maturity of the states' fiscal management processes and opportunities for strengthening them.[42] Another key lesson was the importance of advance planning to implement complex outputs. In this connection, it was agreed with the executing agencies that the technical specifications and terms of reference, mainly for the technological innovation outputs, will be prepared as a priority before the start of execution with support from specialized consulting services in information technology, expenditure, and revenue.

b. **Development.** Participation by representatives of the project coordination unit (PCU) of the states in the Network of the Treasury Management Commission

[37] Loans 1194/OC-BR, 2248/OC-BR, and 3391/OC-BR.

[38] Federal Revenue Service (SRF), 1996.

[39] Loan 3142/OC-BR.

[40] PROFISCO I – PB PCR.

[41] Midterm evaluation and PCR of seven states (Minas Gerais, Rio de Janeiro, Piauí, Mato Grosso, Maranhão, Pernambuco, and Rio Grande do Norte).

[42] Inter-American Center of Tax Administrations (CIAT), 2017.

(COGEF) fostered the sharing of fiscal management modernization experiences and solutions with other states.

c. **Execution.** To compensate for delays in execution, the Bank created a monitoring tool known as the Execution Acceleration Plan, which uses the progress monitoring report (PMR) to identify delayed outputs and prepares mitigation measures until execution is normalized.

d. **Evaluation.** The difficulty of evaluating projects given a very large number of indicators that differ across individual projects. This issue was resolved in PROFISCO II, because individual projects have one relevant outcome indicator for each component, and the indicators are the same for all individual projects.

e. **Results.** The SPED—including the NF-e, digital tax accounting (EFD), and digital bookkeeping system—was identified as one of the outputs that contributed the most to increasing the efficiency of the states' fiscal controls.[43] By automating the flow of information between taxpayers and the state, the SPED exponentially increases the information available for audit, which makes it more likely that a tax offense will be detected and sanctioned and thus heightens the perception of risk among taxpayers. PROFISCO II will invest in further development of the SPED and seek to exploit its potential by expanding the information it generates to automate tax auditing[44] and simplify tax compliance, among other actions, leveraging the new technologies of the digital economy.

f. **PROFISCO I – PB.** The PROFISCO I – PB project completion report (PCR) identified the following factors as having a negative impact on project execution: (i) difficulty in developing and implementing outputs, owing to lack of previous experience in project execution and communication with the different actors involved; (ii) difficulty in preparing terms of reference and monitoring their implementation; and (iii) difficulty in implementing a large number of outputs. This project includes actions to: (i) maintain the structure and staff of the PCU that implemented PROFISCO I, with additional measures to improve coordination and communication among output leaders and train key actors in project management and Bank policies; (ii) hire support for preparation of terms of reference and training in project management; and (iii) reduce the number of outputs and consolidate procurement processes. In addition, actions are also proposed to: (i) ensure the sustainability of the outcome achieved by including outputs related to improving the quality of public expenditure and increasing the effectiveness of tax collection; and (ii) ensure the sustainability of information technology investments by planning and prioritizing resources for the updating and maintenance of data infrastructure and security.

1.20 **The Bank's experience in other countries of the region.** This operation draws on the Bank's recent experiences with tax administration reforms in Costa Rica (loan 4819/OC-CR), Ecuador (loan 3325/OC-EC), El Salvador (loan 3852/OC-ES),

[43] McKinsey & Company, 2014: NF-e and SPED made it more likely that tax evaders would be identified and thus helped reduce the informality of employment in Brazil in the last ten years (from 55% to 40%).

[44] Araujo, 2013: The use of the SPED and artificial intelligence will increase the identification of tax fraud.

Honduras (loan 3541/BL-HO), Jamaica (loan 2658/OC-JA), and Peru (loan 3214/OC-PE); financial management system modernization in Guyana (loans 1550/SF-GY and 1551/SF-GY), Honduras (loan 2032/BL-HO), and Nicaragua (loan 2422/BL-NI); and public investment management in Argentina (loan 3835/OC-AR), Bolivia (loan 3534/BL-BO), Chile (loan 1281/OC-CH), Ecuador (loan 2585/OC-EC), Mexico (loan 2550/OC-ME), Paraguay (loan 3628/OC-PR), Panama (loan 2568/OC-PN), and Peru (loan 2703/OC-PE). These experiences emphasize that: (i) the focus of the reforms should be on improving the entities' business models; (ii) the very large-scale utilization of digital intelligence and risk analysis in data processing makes tax audits more effective; (iii) the utilization of state-of-the-art technology (such as big data) makes it possible to process large volumes of data; and (iv) the human capital of the entities is the most important asset to be considered in any reform.

1.21 **International evidence.** Empirical evidence shows that fiscal discipline and sustainability are closely related to strong fiscal institutions.[45] Banerjee et al. (2017) report reductions in program implementation costs when governments leverage technology. Dhaliwal and Hanna (2014) find that automated programs for monitoring processes can result in more efficient use of public resources and enhance service quality. Arenas de Mesa (2016) shows the relationship between the sustainability of public finances and the institutional framework for fiscal management and transparency.

1.22 On the taxation side, recent evaluations show that revenue performance responds significantly to institutional strengthening of tax administrations: (i) improvement of the accessibility and quality of available information;[46] (ii) information-intensive audit models;[47] (iii) simplified procedures to facilitate tax compliance;[48] and (iv) strategies to ensure that human resources are adequately qualified and motivated.[49] Several tax administrations in Latin America have strengthened these factors, particularly those of Brazil and Uruguay.[50]

1.23 Moreover, in relation to public expenditure, several different studies point to the need for actions to improve technical and allocative efficiency with a view to fostering fiscal sustainability, equity, and economic growth.[51] In this connection, it is crucial to improve public procurement through:[52] strategic procurement planning, the use of electronic systems, systematic monitoring, and information transparency. In

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45 Poterba, James M., and Jürgen von Hagen. Fiscal Institutions and Fiscal Performance. University of Chicago Press, 1999; and Alesina, A., et al. "Budget Institutions and Fiscal Performance in Latin America." Journal of Development Economics (1999): 253-273.

46 Evasion rates are up to eight times higher where the tax administration lacks automated tools to verify taxpayers' income sources (Slemrod et al., 2015; Pomeranz, 2015; Kleven et al., 2011).

47 Information availability complements company audits in Spain (Almunia and López Rodriguez, 2016).

48 This can raise payment rates by up to four percentage points (Hallsworth et al., 2014).

49 Incentive schemes for key tax administration staff to generate additional revenue produced rates of return of between 35% and 51% (Khan et al., 2016).

50 Loan 1783/OC-UR PCR. Barreix and Zambrano (2018). Electronic Invoicing in Latin America. IDB. The "Nota Fiscal Paulista" program increased ICMS revenue by US$226 million.

51 Better Spending for Better Lives (2019).

52 Better Spending for Better Lives (2019): Inefficiencies in public procurement cost around 1.4% of GDP in Latin America and the Caribbean.

addition, the strengthening of public investment management can increase the potential benefits on economic and social development by up to 30%.[53] [54] In Latin America, countries with more developed national public investment systems report greater efficiency.[55] International experience also shows that the adoption of a medium-term budgetary framework (MTBF), which creates a link between current budgetary decisions and their medium-term implications, has a positive impact on fiscal sustainability.[56] Most countries of the Organisation for Economic Co-operation and Development (OECD) have implemented this tool, and, in recent decades, several Latin American countries have also adopted it.[57] Countries that have a strong MTBF tend to be more effective in achieving their fiscal targets.[58]

1.24 **Strategic alignment.** The program is consistent with the second Update to the Institutional Strategy (document AB-3190-2). It is strategically aligned with the development challenge of productivity and innovation by reducing tax collection costs through the use of information and digital technology, and with the crosscutting themes of institutional capacity and rule of law by strengthening tax systems and public resource management and planning systems, and climate change and environmental sustainability. According to the multilateral development banks' joint methodology, this operation has 14.7% climate finance content due to the purchase of efficient equipment that reduces energy consumption and greenhouse gas emissions, as well as the integration of climate change parameters into the state's public investment model. These resources contribute to the IDB Group's goal of increasing the financing of climate change-related projects to 30% of the volume of approvals by 2020. The program also contributes to the IDB Group Corporate Results Framework 2020-2023 (document GN-2727-12) through the following indicators: (i) percent of GDP collected in taxes; (ii) government agencies benefited by projects that strengthen technological and managerial tools to improve public service delivery by strengthening the integrated tax administration system, financial system, and integrated administrative management system; (iii) subnational governments benefited by decentralization, fiscal management, and institutional capacity projects; (iv) countries using country fiduciary systems; and (v) accountability institutions strengthened. It is also aligned with the Sector Strategy: Institutions for Growth and Social Welfare (document GN-2587-2) and is consistent with the following sector framework documents: Decentralization and Subnational Governments (document GN-2813-8), and Fiscal Policy and Management (document GN-2831-8), along the following dimensions: (i) improve expenditure quality and efficiency and service delivery; (ii) increase tax revenue intake; and (iii) promote greater transparency and accountability. The program is also consistent with the Climate Change Sector Framework Document (document GN-2835-8) by reducing greenhouse gas emissions through the procurement of efficient equipment, as well as by integrating climate change indicators in the prioritization of public investment.

53 IMF (2015).

54 Calderón and Servén (2004); Gupta et al. IMF (2014).

55 Armendariz and Contreras (2016).

56 World Bank (2013; 1998).

57 World Bank (2013). For Latin America and the Caribbean, see IDB (2009).

58 IMF (2013); World Bank (2013).

1.25 **The Bank's country strategy.** The project is aligned with the IDB Group 2019-2022 Country Strategy with Brazil 2019-2022 (document GN-2973), specifically through the following strategic objectives: (i) reform the structure of public expenditure (Components 1 and 3); (ii) perfect the public investment system (Component 3); and (iii) promote e-government and digital solutions to foster transparency, accountability, and efficiency in delivering services to citizens and enterprises (Components 1, 2, and 3). Lastly, the operation is included in the 2020 Operational Program Report (document GN-2991-1).

B. Objectives, components, and cost

1.26 The project objective is to contribute to the fiscal sustainability of the State of Paraíba through the following specific objectives: (i) modernization of fiscal management; (ii) improvement of tax administration, and (iii) improvement of public expenditure management. This operation will finance the following components:

1.27 **Component 1. Financial management and fiscal transparency (US$21,242,000).** This component seeks to improve management processes and instruments, modernize the technology infrastructure, and make the tax administration more transparent to the general public, by enhancing the institutional performance of the agencies involved the state's fiscal management. It will finance the following activities:

a. **State strategic management model (US$2,210,373)**, including: (i) a state governance strategy; (ii) a strategic plan for the fiscal management institutions; (iii) a fiscal management risk methodology; (iv) a methodology for managing the indicator targets of the multiyear plan / Annual Budget Law (LOA); (v) an internal audit methodology; (vi) a state civil service integrity program; and (vii) an integrated internal control system.

b. **Personnel management model for fiscal management institutions (US$918,908)**, including: (i) a skills-based personnel management procedure; (ii) a program to harness innovation and knowledge management; (iii) a performance evaluation methodology; and (iv) an ongoing training plan.

c. **Information technology model (US$12,174,450)**,[59] including: (i) an information technology master plan; (ii) an ICT training plan; (iii) a fiscal management services control center; (iv) expansion of the hardware and software infrastructure; (v) automated corporate systems using new technologies; (vi) a corporate data center with a cybersecurity solution to enhance data security; and (vii) an electronic tax document management system.

d. **Procurement management model (US$4,191,350)**, including: (i) a government procurement strategic planning methodology; and (ii) a government procurement portal integrated with the management systems.

e. **Fiscal citizenship and transparency model (US$1,746,919)**, including: (i) a citizen services portal; (ii) a transparency portal; (iii) integrated protocol

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[59] At least 70% of equipment purchases must meet energy efficiency criteria such as those of Procel, Energy Star, or equivalent labels.

systems of the fiscal management institutions; and (iv) an enhanced fiscal education program.

1.28 **Component 2. Tax administration and litigation (US$10,107,000).** This component seeks to make tax administration and litigation management more efficient, grow revenues, and simplify tax compliance. It will finance the following activities:

a. **Tax policy management model (US$385,000)**, including: (i) a methodology for subsidizing tax policy formulation and monitoring; (ii) procedures for the granting and control of tax concessions; (iii) a methodology for estimating the fiscal gap; and (iv) a system for consulting tax legislation and issues using artificial intelligence.

b. **Economic and fiscal information management model (US$924,000)**, including (i) the system of the National Network for Simplified Registration and Legalization of Businesses and Firms (REDESIM), including a taxpayer registration management dashboard; (ii) a module for integration to the foreign trade single portal; (iii) a management system for calculating the municipal revenue sharing index (IPM); (iv) a procedure for simplifying ancillary tax obligations of the state goods and services sales tax (ICMS); and (v) a system for tracking taxpayers under the "Simples Nacional" simplified tax regime.

c. **Tax intelligence and inspection model (US$5,718,000)**, including: (i) a system for inspections of goods in transit; (ii) a system of mass electronic auditing for all types of taxpayers, including audit planning actions for state taxes; and (iii) a tax intelligence procedure using big data and artificial intelligence.

d. **Tax litigation management model (US$1,630,000)**, including (i) procedures for administrative and judicial actions (from inspection to prosecution); (ii) an integrated administrative and judicial e-process system; and (iii) a Tax Transaction and Conciliation Service within the Office of the State Attorney General (PGE/PB).

e. **Taxpayer services model (US$1,064,000)**, including (i) a taxpayer service center using digital tools; (ii) electronic address for tax purposes; and (iii) on-site service centers with adequate physical and technological infrastructure.

f. **Revenue assessment and collection management model (US$386,000)**, including an administrative claim collection system with taxpayer risk management procedures and new debt financing procedures.

1.29 **Component 3. Financial administration and public expenditure quality (US$10,931,000).** This component seeks to strengthen fiscal discipline and make public expenditure more efficient and effective. It will finance the following activities:

a. **Government public policy management model (US$592,000)**, including (i) a methodology for monitoring government programs and actions, including integration and customization of the existing digital platform; and (ii) a public policy management training plan.

b. **Financial execution management model (US$550,000)**, including: (i) automated Treasury cash flow; and (ii) financial execution control procedures.

c. **Supervision model for state-owned enterprises (US$153,649)**, including: (i) a supervision methodology; (ii) an automated system to support supervision; and (iii) a public enterprise management training plan.

d. **Accounting and cost management model (US$9,128,865)**, including: (i) an accounting convergence process; (ii) identification, inventory, and revaluation of the state's real estate assets; and (iii) a public cost methodology.

e. **Public debt management model (US$185,000)**, including: (i) a debt control procedure for government departments and decentralized agencies, public and semipublic enterprises, and public foundations, including existing and contingent liabilities and identifying fiscal risks; and (ii) an integrated government debt tracking system integrated with the Integrated Financial Administration System (SIAF).

f. **State public investment model (US$321,486)**, including (i) systematized procedures for public investment management at the Planning, Budget, and Management Department (SEPLAG); (ii) a system for identifying and prioritizing public investment based on the state's socioeconomic and climate-change vulnerability indicators; (iii) a methodology for preparing projects and feasibility studies; (iv) technical studies for pre-investment projects; and (v) a project monitoring and evaluation methodology with a computerized support system.

1.30 **Project management (US$400,000).** The project will also finance the activities to support project administration and execution, including the costs of financial and accounting audits and monitoring and evaluation.

1.31 The project will finance the following investment categories for all components: (i) training US$2,235,568 (5%); (ii) consulting services US$9,588,973 (22%); (iii) goods US$13,839,617 (32%); (iv) nonconsulting services US$8,723,249 (20%); and (v) renovations of existing buildings US$8,292,593 (19%).

1.32 **Beneficiaries.** The state of Paraíba's greater fiscal sustainability will benefit its citizens, businesses, taxpayers, and public and nongovernmental entities through better service delivery, facilities, and lower costs for tax compliance, as well as more readily available information for government management and accountability.

C. Key results indicators

1.33 The expected impacts are: (i) an increase in the ratio of the state's tax revenue intake to GDP; (ii) a decrease in the ratio of the state's primary fiscal deficit to GDP; and (iii) a decrease in the ratio of the state's net current debt to GDP. The expected outcomes are: (i) an increase in the ratio of strategic planning goals met to total planned goals; (ii) a decrease in SEFAZ/PB's ratio of administrative cost of tax collection to total revenue intake; and (iii) a narrowing of the gap between the budget as planned and as executed.

1.34 **Cost-effectiveness analysis.** A cost-effectiveness analysis was done to estimate the project's effectiveness relative to three other PROFISCO I projects, the results

of which were evaluated using their project completion reports (PCRs) and found to be satisfactory. The variables used were the project costs and the tax administration revenue collection efficiency index.[60] The analysis estimated that, with implementation of the project, Paraíba will attain an efficiency index of 3.51%, representing an increase in effectiveness of 22.53%, which is higher than the 17.19% average of the three comparator states. In terms of sensitivity, Paraíba needs to attain an efficiency index of at least 3.55% to achieve effectiveness of 20.53%.[61]

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instruments

2.1 This operation was designed as a specific investment loan under the PROFISCO II CCLIP (BR-X1039). Its total cost of US$42,680,000 will be financed with US$38,412,000 from the Bank's Ordinary Capital resources and a local counterpart contribution of US$4,268,000. The distribution of resources by source of financing and category is shown in Table 1.

Table 1. Total budget (US$)

Categories	IDB	Local	Total	%
Direct costs	**38,012,000**	**4,268,000**	**42,280,000**	**99.06**
Component 1. Fiscal management and transparency	21,242,000	-	21,242,000	**49.8**
Component 2. Tax administration and litigation	10,107,000	-	10,107,000	**23.7**
Component 3. Financial administration and public expenditure quality	6,663,000	4,268,000	10,931,000	**25.6**
Project management	**400,000**	**-**	**400,000**	**0.94**
Total	**38,412,000**	**4,268,000**	**42,680,000**	**100**
%	**90**	**10**	**100**	

2.2 **Disbursement schedule.** Disbursements will be made over a five-year period as shown in Table 2:

Table 2. Disbursement schedule (US$)

Sources	Year 1	Year 2	Year 3	Year 4	Year 5	Total
IDB	3,613,869	7,176,523	12,614,507	10,775,010	4,232,092	38,412,000
Local	426,800	853,600	853,600	2,134,000	0.00	4,268,000
Total	**4,040,669**	**8,030,123**	**13,468,107**	**12,909,010**	**4,232,092**	**42,680,000**
%	**9**	**19**	**32**	**30**	**10**	**100%**

2.3 **Compliance with the eligibility conditions for the PROFISCO II CCLIP (BR-X1039).** The project meets the eligibility criteria of the CCLIP policy (document

[60] The efficiency index is measured as the ratio of the administrative cost of tax collection to total tax revenue intake. The lower the index, the better the result.

[61] Mean cost-effectiveness was also compared.

GN-2246-9)[62] for individual loan operations, given that: (i) the project falls under the fiscal sector and is compatible with all the components defined under the PROFISCO II CCLIP; (ii) the operation is included in the 2020 Operational Program Report (document GN-2991-1); (iii) the state will implement the operation through the State of Paraíba Finance Department (SEFAZ/PB), which was the same executing agency as for the PROFISCO I – PB individual operation (loan 2184/OC-BR); (iv) the state satisfactorily executed the PROFISCO I – PB project, achieving the objectives envisaged; and (v) the findings of the institutional analysis show that the performance level of SEFAZ/PB has not deteriorated, and the same project execution and monitoring tools can be used for this new operation as for the previous one. The project coordination unit (PCU) staff will be the same. The PROFISCO I – PB project completion report showed that: (i) the project objectives were satisfactorily achieved; and (ii) the executing agency met the requirements of the Loan Contract and the Bank's disbursement policies, and its accounts were audited and found to meet the required quality standards.

B. Environmental and social safeguard risks

2.4 In accordance with the Bank's Environment and Safeguards Compliance Policy (Operational Policy OP-703), the project is classified as category "C." The project will support the strengthening of financial and taxation processes. It will not finance infrastructure works or the purchase of land, only renovations and modernizations of existing facilities. Accordingly, no socioenvironmental risks are foreseen.

C. Fiduciary risks

2.5 The following medium-high risk was identified: If SEFAZ/PB has no flexible mechanism in place for reviewing the project's procurement processes, they will be reviewed by the State Procurement Center without the necessary priority, jeopardizing project execution. This risk will be mitigated by creating a special committee at the State Procurement Center, or a Special Bidding Committee at SEFAZ/PB, which will prioritize execution of the project's procurement processes.

D. Other key risks and issues

2.6 A risk management workshop was held following the Bank's methodology. The risk of the operation was rated as medium, with the following risks being identified:

a. **Public management and governance.** The following are classified as medium-high-risks: (i) if there are changes of authorities at any of the fiscal management agencies, priorities may also change in the implementation of outputs, leading to delays in the project execution timetable. This risk will be mitigated by creating a coordination committee with the five agencies involved (SEPLAG, CGE/PB, PGE/PB, SEAD, and SEFAZ/PB), to ensure project governance (see paragraph 3.3); and (ii) if there are difficulties in assembling technical teams to implement the project outputs, the existing team may become overloaded, leading to delays in the project execution timetable. This risk will be mitigated by engaging individual consultants to support SEFAZ/PB

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[62] This operation has been prepared in accordance with the eligibility criteria specified in document GN-2246-9, pursuant to the provisions of paragraph 3.12 of document GN-2246-13.

staff in technical areas of income and expenditure, as necessary, throughout project execution.

b. **Fiscal sustainability.** There is a medium-high risk that, if the adverse impact of the COVID-19 pandemic continues to evolve, the impact on the Brazilian economy will be severe, especially at the subnational level, which may affect the state's ability to contribute the counterpart funding, jeopardizing the achievement of project results. This risk will be mitigated by adjusting the project's financial timetable to allow execution with a higher proportion of Bank resources during the period when the state is having difficulty contributing the counterpart.

c. **Development.** There is a medium-high risk that, if the teams responsible for preparing the terms of reference and technical specifications do not have the required technical capacity to identify the solutions or are not trained to prepare the documents in the required formats, the solutions implemented will not satisfy the quality criteria, and the project objectives may not be met. This risk will be mitigated by hiring specialized consulting services in information technology issues (funded under project management), to support SEFAZ/PB staff in preparing the terms of reference and technical specifications.

d. **Sustainability.** There is a medium-high risk that, if after project-end resources are insufficient to maintain the quality of the outputs and the performance of outcomes, the implemented outputs may deteriorate, affecting the performance of the state's public financial management. This risk will be mitigated by: (i) implementing an ongoing training plan for permanent technical staff that will ensure continuity of the quality of the implemented procedures (see paragraph b); and (ii) implementing the ICT Master Plan, setting aside the necessary resources and identifying sources of funding to maintain the equipment and solutions (see paragraph c).

2.7 **Fiscal analysis of the state.** The analysis of Paraíba's financial condition confirms its ability to pay for servicing the debt incurred with this loan, which represents approximately 0.2% of the state's GDP and just 1.6% of net current income (NCI) for 2018. Moreover, the state has a "B" rating, the second best issued by the National Treasury Department (STN) using the "ability to pay" (CAPAG) methodology, which demonstrates its fiscal capacity. Paraíba has also been complying with the Fiscal Responsibility Law and with the conditions specified by the Fiscal Adjustment Program (see State of Paraíba fiscal analysis).

2.8 **Program sustainability.** To ensure that the capabilities generated by the project are sustainable after execution has ended, the following outputs are envisaged that with the expected improvement in the economy and in the state's fiscal condition will contribute to more efficient tax administration and public expenditure, leading to higher levels of revenue intake and savings in state procurement: (i) tax compliance and intelligence, which will make it possible to identify a larger number of potential evaders and encourage them to stay in compliance; (ii) control of expenditure ceilings, which will make it possible to comply with financial programming and consequently improve the use of public resources; and (iii) a public investment model, which will enable the state to invest in priority areas by leveraging its economic growth. With regard to investments in technology, SEFAZ/PB will mainly use its permanent staff in conjunction with consulting services to support the

necessary development and maintenance. The project will finance improved data protection and cybersecurity measures.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

3.1 The borrower is the State of Paraíba, which will execute the operation through the State of Paraíba Finance Department (SEFAZ/PB). The Federative Republic of Brazil will be guarantor of the borrower's financial obligations, pursuant to the policy on Guarantees Required from the Borrower (document GP-104-2). A project coordination unit (PCU) will be established for project execution, staffed by a general coordinator, a technical coordinator, an administrative/financial coordinator, a planning and monitoring adviser, and a procurement adviser. The PCU will coordinate project planning, monitoring, evaluation, and audit activities.

3.2 The PCU's main functions will be to: (i) plan the execution of activities; (ii) prepare, implement, and update the project's operational tools: multiyear execution plan, annual work plan, procurement plan, monitoring and evaluation plan; (iii) supervise execution and deliver status reports; (iv) coordinate and support processes for the preparation of terms of reference, procurement of goods, and selection and contracting of services; (v) submit justifications and disbursement requests to the Bank; (vi) prepare financial statements; and (vii) submit the project evaluation. The borrower will adhere to the program Operating Regulations approved by the Bank for the PROFISCO II CCLIP, which specify: (i) the criteria for projects and outputs to be eligible for financing; (ii) the functions, procedures, and rules for project execution; and (iii) the operational and contractual relationships between the parties involved in the project.

3.3 **Interagency coordination mechanism.** SEFAZ/PB will cooperate with the Planning, Budget, and Management Department (SEPLAG), the Office of the State Comptroller General (CGE/PB), the Office of the State Attorney General (PGE/PB), and the Administration Department (SEAD) for the execution of activities benefiting them. These entities will appoint output leaders, who will coordinate their actions with the PCU and ensure their technical development and implementation. For the coordination of procurement activities related to human resource management, procurement, public expenditure, tax litigation, internal control, and communication with society, the information flows and processes between the beneficiaries will be mapped and defined to identify roles, responsibilities, and timing, which will be institutionalized through cooperation instruments (see paragraph 3.5).

3.4 **Special contractual conditions precedent to the first disbursement of the loan: (i) the borrower will adhere to the program Operating Regulations previously approved by the Bank for all individual operations under the PROFISCO II CCLIP.** This condition is justified in view of the operational, fiduciary, and institutional responsibility rules and regulations that will be required, to ensure orderly project startup and implementation. The program Operating Regulations will be reviewed periodically and may be modified with the express approval of the Bank; **and (ii) the PCU has been established, and its members appointed**. This condition is justified in view of the need to formally establish the PCU, to mitigate the risk of delay in

project implementation and to conduct the project's operational and fiduciary processes exclusively and with the necessary experience.

3.5 **Special contractual conditions for execution.** Prior to the start of execution of activities with outputs intended for the Planning, Budget, and Management Department (SEPLAG), the Administration Department (SEAD), the Office of the State Comptroller General (CGE/PB), and the Office of the State Attorney General (PGE/PB), SEFAZ/PB will sign a legal instrument with those entities of the borrower, to establish the roles and responsibilities of the parties during execution of the respective activities. This condition is justified by the need to ensure that the entities benefiting from the activities will provide the necessary cooperation to SEFAZ/PB, which will be in charge of executing them.

3.6 **Procurement.** Procurement processes will be conducted by a Special Bidding Committee designated for the program with sufficient capacity to meet demand. Procurement and contracting will be in accordance with the Policies for the Procurement of Goods and Works Financed by the IDB (document GN-2349-15) and the Policies for the Selection and Contracting of Consultants Financed by the IDB (document GN-2350-15), and as specified in the procurement plan.

3.7 **Direct contracting.** Based on the provisions of policy document GN-2350-15 governing the direct selection of consulting firms (see paragraph 3.11d), the following entities will be engaged via single-source selection: (i) the National School of Public Administration of the Ministry of Economy (ENAP/ME), the state government schools, federal and state universities, and data processing firms that provide training to civil servants and technical assistance for IT development; and (ii) the Inter-American Center of Tax Administrations (CIAT), an international organization, given its specialization in technical assistance to modernize the tax administrations of the region. This is justified due to their unique and exceptional nature as public education and research centers (see Annex III, Chapter IV).

3.8 **Audited financial statements.** The borrower will deliver the project's audited financial statements to the Bank annually, within the first 120 days after the close of each fiscal year. The audit will be performed by independent consultants contracted with loan proceeds.

B. Summary of arrangements for monitoring results

3.9 **Monitoring.** Monitoring will be based on the following instruments: (i) the multiyear execution plan and annual work plan; (ii) the procurement plan; (iii) the Results Matrix; and (iv) the monitoring and evaluation plan. The executing agency will submit the updated versions of instruments (i) and (ii) to the Bank by 30 November of each year. The PCU will prepare six-monthly reports on progress toward the outcomes, outputs, and financial targets for the Bank's approval. The Bank will conduct inspection visits and ex post reviews as part of project monitoring.

3.10 **Evaluation.** The project will be evaluated against the annual outcome and output targets and indicators contained in the project's Results Matrix by before-and-after comparison of results. The monitoring and evaluation plan calls for an independent midterm evaluation and a final evaluation. The independent midterm evaluation will be delivered 90 days after 36 months have elapsed since the loan contract signature date, or the date on which 50% of the loan proceeds have been disbursed, whichever occurs first. The final evaluation will be delivered 90 days after the date

of the last disbursement. The evaluation reports will serve as inputs for the project completion report (PCR).

Development Effectiveness Matrix		
Summary	**BR-L1535**	
I. Corporate and Country Priorities		
1. IDB Development Objectives		
Development Challenges & Cross-cutting Themes	**-Productivity and Innovation -Climate Change and Environmental Sustainability -Institutional Capacity and the Rule of Law**	
Country Development Results Indicators	**-Percent of GDP collected in taxes (%) -Government agencies benefited by projects that strengthen technological and managerial tools to improve public service delivery (#)* -Subnational governments benefited by decentralization, fiscal management and institutional capacity projects (#)* -Countries that use fiduciary country systems (#)* -Accountability institutions strengthened (#)***	
2. Country Development Objectives		
Country Strategy Results Matrix	**GN-2973**	**(i) Reform the structure of public expenditure; (ii) Perfect the public investment system; (iii) Promote e-government and digital solutions to foster transparency, accountability, and efficiency in delivering public services to citizens and enterprises.**
Country Program Results Matrix	**GN-2991-1**	**The intervention is included in the 2020 Operational Program.**
Relevance of this project to country development challenges (If not aligned to country strategy or country program)		
II. Development Outcomes - Evaluability		**Evaluable**
3. Evidence-based Assessment & Solution	**9.1**	
3.1 Program Diagnosis	**3.0**	
3.2 Proposed Interventions or Solutions	**4.0**	
3.3 Results Matrix Quality	**2.1**	
4. Ex ante Economic Analysis	**8.6**	
4.1 Program has an ERR/NPV, or key outcomes identified for CEA	**2.2**	
4.2 Identified and Quantified Benefits and Costs	**3.3**	
4.3 Reasonable Assumptions	**1.0**	
4.4 Sensitivity Analysis	**2.2**	
4.5 Consistency with results matrix	**0.0**	
5. Monitoring and Evaluation	**8.3**	
5.1 Monitoring Mechanisms	**1.4**	
5.2 Evaluation Plan	**6.8**	
III. Risks & Mitigation Monitoring Matrix		
Overall risks rate = magnitude of risks*likelihood	**Medium**	
Identified risks have been rated for magnitude and likelihood	**Yes**	
Mitigation measures have been identified for major risks	**Yes**	
Mitigation measures have indicators for tracking their implementation	**Yes**	
Environmental & social risk classification	**C**	
IV. IDB´s Role - Additionality		
The project relies on the use of country systems		
Fiduciary (VPC/FMP Criteria)	**Yes**	**Financial Management: Budget, Treasury, Accounting and Reporting. Procurement: Information System, Price Comparison.**
Non-Fiduciary	**Yes**	**Statistics National System.**
The IDB's involvement promotes additional improvements of the intended beneficiaries and/or public sector entity in the following dimensions:		
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project	**Yes**	**The IDB team developed and applied a methodology to assess the state of public finances and fiscal management processes in the State of Paraiba to design the project and monitor future performance relative to the baseline. (MDGFIS).**

Note: (*) Indicates contribution to the corresponding CRF's Country Development Results Indicator.

Evaluability Assessment Note:
The main goal of the operation is to contribute to the fiscal sustainability of the State of Paraiba. To achieve this end, the proposal defines three specific areas on which the project will intervene. The first area is fiscal management. The second area is tax administration. The third area is the administration of public expenditure. Each of these areas is associated to a component. The document includes a description of the process gaps that lead to weaknesses in each of these three areas. The project is the child of a series of operations under the Conditional Credit Line for Investment Projects (CCLIP) parent BR-X1039.

The project proposal diagnoses a primary balance as a share of the State PIB of 0.4 percent in 2019, and a Current Net Debt as a share of the State PIB of 4.0 Percent in 2018 (SEFAZ, 2019). The diagnosis is based on the MD-GEFIS tool which analyzes processes in the three main areas which define the components. The Ministry of Finance provides a diagnosis for a total of 21 sub areas. Each diagnosis identified the main restrictions for the Ministry to increase tax revenue, decrease running costs or improve efficiency in expenditures, and improve service delivery to citizens. Overall, the diagnosis identifies gaps in institutional arrangements (such as weak coordination and outdated legal documents), deficits in personnel management and training, and gaps in capital investments (resulting in outdated technological infrastructure, limited availability of information, and lack of mechanisms to communicate with citizens). The quantification of these needs is disaggregated for 17 processes.

The economic analysis provides a cost-effectiveness comparison of reducing tax evasion as compared to the states of Mato Grosso do Sul, Piaui, and Pernambuco. The analysis concludes Paraiba has potential to decrease the cost per dollar collected by 23 percent compared to decreases of 5 percent for Mato Grosso do Sul, 33 percent for Piaui, and 14 percent for Pernambuco.

Monitoring relies on reports by the Finance Secretariat and the Ministry of Planning of the State. The ex post evaluation plan includes an impact evaluation to identify the effects of a monitoring system of transit merchandise on tax collection and the efficiency of the process. The evaluation relies on a randomized control trial.

The project identifies nine risks out of which six are classified as medium high and three as medium low. The risk classified as medium high include changes of priorities by the local government, technical restrictions to deliver products, the impact of COVID-19 on the economy of the state, lack of resources for product maintenance, and weak procurement processes.

RESULTS MATRIX[1]

Project objective:	The project objective is to contribute to the fiscal sustainability of the State of Paraíba through the following specific objectives: (i) modernization of fiscal management; (ii) improvement of tax administration, and (iii) improvement of public expenditure management.

GENERAL DEVELOPMENT OBJECTIVE

Indicator	Unit of measure	Baseline	Base year	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
General development objective: The principal objective is to contribute to the fiscal sustainability of the State of Paraíba											
Paraíba state primary balance/GDP	%	0.37	2019	0.27	0.24	0.10	0.05	0.04	0.04	State balance sheet data report	See monitoring and evaluation plan (MEP)
Paraíba state tax revenue intake/GDP	%	9.19	2019	9.19	9.19	9.54	9.90	10.27	10.27	Revenue collection operational management report – Operations Monitoring Unit (GOA) of the State of Paraíba Finance Department (SEFAZ/PB)	See MEP
Paraíba state net current debt/GDP	%	4.03	2018	3.56	3.19	2.90	2.65	2.50	2.50	State balance sheet data report	See MEP

[1] The targets initially set have not taken the pandemic into account, so the figures included for the impact indicators may be recalculated considering the current context of COVID-19.

SPECIFIC DEVELOPMENT OBJECTIVES

Indicator	Unit of Measure	Baseline	Base year	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
Specific objective 1: Modernization of fiscal management											
Number of goals met/ total planned goals	%	62.5	2018	65	70	75	80	87.5	87.5	Information produced by the SEFAZ/PB Planning Division	See MEP
Specific objective 2: Improvement of tax administration											
Cost of tax collection/ total revenue intake	%	4.53	2019	4.53	4.53	4.16	3.82	3.51	3.51	State's general balance sheet produced by SEFAZ/PB	See MEP
Specific objective 3: Improvement of public expenditure management											
Budget as executed/ budget as planned	%	2.36	2018	2.30	2.20	2.10	2.05	2.00	2.00	State's budget execution report produced by SEFAZ/PB	**Calculation formula:** Budget as planned/Budget as executed **Baseline: 2.36%**. Budget as planned = R$10,762,006,466 Budget as executed = R$10,507,521,304

OUTPUTS[1 2]

Indicator	Unit of measure	Baseline	Base year	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
Component 1. Fiscal management and transparency											
1.1 State strategic management model implemented[3]	Model	0	2019	0	0	0	0	1	1	Planning Department (SEPLAG) management report	See MEP For the information technology model, 70% of the hardware procurement budget will be spent on equipment with energy efficiency labeling.
1.2 Personnel management model for fiscal management institutions implemented	Model	0	2019	0	0	0	0	1	1	SEFAZ Human Resources Office management report	
1.3 Information technology model implemented	Model	0	2019	0	0	0	0	1	1	SEFAZ Information Technology Office management report	
1.4 Procurement management model implemented[4]	Model	0	2019	0	0	0	1	0	1	SEFAZ Administration Office management report	
1.5 Fiscal citizenship and transparency model implemented	Model	0	2019	0	0	0	0	1	1	SEFAZ Fiscal Education management report	

1 The results are cumulative.

2 Systems, models, or software will only be considered complete once up and running and in use by public officials.

3 Model is a set of activities that may include: (i) diagnostic assessment of the current state of affairs; (ii) a methodology and change proposal; (iii) process reengineering; (iv) an information technology solution; and (v) training on new processes and tools.

4 At least 70% of equipment purchases must satisfy energy efficiency criteria such as Procel, Energy Star, or equivalent labels.

Indicator	Unit of measure	Baseline	Base year	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
Component 2. Tax administration and litigation											
2.1 Tax policy management model implemented	Instruments	0	2019	0	0	2	2	0	4	SEFAZ Economic and Fiscal Studies Office management report	See MEP
2.2 Economic and fiscal information management model implemented	Model	0	2019	0	0	0	1	0	1	SEFAZ Economic Information Office management report	
2.3 Tax intelligence and inspection model implemented	Model	0	2019	0	0	0	1	0	1	SEFAZ Audit Office management report	
2.4 Tax litigation management model implemented	Model	0	2019	0	0	0	1	0	1	SEFAZ Litigation Office management report	
2.5 Taxpayer service model implemented	Model	0	2019	0	0	0	0	1	1	SEFAZ Taxpayer Service Office management report	
2.6 Revenue collection management model implemented	Model	0	2019	0	0	0	1	0	1	SEFAZ revenue collection management report	

Indicator	Unit of measure	Baseline	Base year	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
Component 3. Financial administration and public expenditure quality											
3.1 Government public policy management model implemented	Model	0	2019	0	0	0	0	1	1	SEPLAG management report	See MEP
3.2 Financial performance management model implemented	Model	0	2019	0	0	1	0	0	1	SEFAZ Treasury Secretariat management report	
3.3 State-owned enterprise financial supervision model implemented	Software	0	2019	0	0	1	0	0	1	SEPLAG management report	
3.4 Accounting and cost management model implemented	Software	0	2019	0	0	0	0	1	1	SEFAZ public accounts management report	
3.5 Public debt management model implemented	Software	0	2019	0	0	0	0	1	1	SEFAZ public debt management report	
3.6 State public investment model implemented	Model	0	2019	0	0	0	0	1	1	SEPLAG management report	

FIDUCIARY AGREEMENTS AND REQUIREMENTS

Country:	Brazil
Project number:	BR-L1535
Project name:	Fiscal Management Modernization Program for the State of Paraíba (PROFISCO II – PB)
Executing agency:	State of Paraíba, acting through its Finance Department (SEFAZ/PB)
Fiduciary team:	David Salazar and Fábia Bueno (VPC/FMP)

I. EXECUTIVE SUMMARY

1.1 The institutional evaluation for the project's fiduciary management was based on: (i) the country's current fiduciary context; (ii) the findings of the evaluation of the main fiduciary risks; (iii) the report of the Fiscal Management Maturity and Performance Assessment (MD-GEFIS); (iv) an institutional analysis; (v) previous experience on PROFISCO I; and (vi) working meetings with the project team and the team at the State of Paraíba Finance Department (SEFAZ/PB).

1.2 Brazil has robust country fiduciary systems enabling sound management of administrative, financial, control, and procurement processes in accordance with the principles of transparency, economy, and efficiency. The executing agency's planning and organization, execution, and control systems have a medium level of development and represent a medium risk.

1.3 SEFAZ/PB has the legal capacity and experience to execute the project activities, since in recent years it has implemented projects with the Bank (PNAF and PROFISCO I) using its own structure with a project coordination unit (PCU). The structure already implemented and consolidated will be used again, drawing on lessons learned from execution of the first phase.

II. FIDUCIARY CONTEXT OF THE EXECUTING AGENCY

2.1 The SEFAZ/PB structure is comprised of units of the Executive Secretariat for Revenue Collection and the Executive Secretariat for Finance.

2.2 The project will benefit the following: SEFAZ/PB as executing agency; the State Planning, Budget, and Management Department (SEPLAG); the Administration Department (SEAD); the Office of the State Attorney General (PGE/PB); and the Office of the State Comptroller General (CGE/PB).

2.3 The project activities will be executed by SEFAZ/PB, acting through its project coordination unit (PCU), which will be responsible for institutional and technical coordination.

2.4 Procurement processes will be conducted by a Special Bidding Committee, created specifically for the program, with sufficient capacity to meet demand generated by it. The executing agency may utilize Banco do Brasil's "Licitacões-e" online bidding system, which is acceptable for procurements using the "Pregão Eletrônico" online reverse auction system.

2.5 The executing agency is subject to both internal and external control. Internal control is exercised by the CGE/PB, and external control by the State of Paraíba Audit Office (TCE/PB), which audits all state entities and is eligible to perform external audits of operations financed with Bank resources.

III. INSTITUTIONAL CAPACITY ASSESSMENT, FIDUCIARY RISK EVALUATION, AND MITIGATION ACTIONS

3.1 The institutional capacity assessment and its validation with SEFAZ/PB staff concluded that the executing agency's institutional capacity is sufficient and adequate with specific opportunities for improvement for the execution of operations with the Bank.

3.2 The following medium-high risk was identified: If SEFAZ/PB has no flexible mechanism in place for reviewing the project's procurement processes, they will be reviewed by the State Procurement Center without the necessary priority, jeopardizing the project execution timetable. This risk will be mitigated by creating a special committee at the State Procurement Center, or a Special Bidding Committee at SEFAZ/PB, which will prioritize execution of the project's procurement processes, as indicated in paragraph 2.4.

IV. AGREEMENTS AND REQUIREMENTS FOR PROCUREMENT EXECUTION

A. Procurement execution

4.1 **Procurement of works, goods and nonconsulting services.** Contracts will be subject to international competitive bidding (ICB) and executed using the standard bidding documents issued by the Bank. Bidding processes subject to national competitive bidding (NCB) will be executed using national bidding documents agreed upon with the Bank.

4.2 **Selection and contracting of consultants.** Consulting contracts will be executed using the standard request for proposals issued by the Bank. Selection and contracting will follow the Policies for the Selection and Contracting of Consultants Financed by the Inter-American Development Bank (document GN-2350-15).

4.3 **Use of the country procurement system.** The country procurement (sub)system approved by the Bank, "Pregão Eletrônico," will be used to purchase of-the-shelf goods in amounts up to US$5 million. Any system or subsystem that may be approved subsequently will be applicable to the operation. The procurement plan and its updates will identify which procurements are to be executed through the approved country systems.

B. Direct contracting and single-source selection

4.4 **Government agencies and schools.** Pursuant to paragraphs 1.13(c) and 3.11 of policy document GN-2350-15, single-source selection will be used to contract the National School of Public Administration of the Ministry of the Economy (ENAP/ME), along with the state government schools, federal and state universities, and data processing firms that provide training to civil servants and technical assistance for IT development, with the aim of making the outputs produced and financed by the project more sustainable. The estimated total value of these contracts is US$1 million.

4.5 **Specialized international agencies.** Pursuant to paragraphs 3.11 and 3.16 of policy document GN-2350-15, single-source selection will also be used to contract the Inter-American Center of Tax Administrations (CIAT) as a specialized agency of exceptional value, since it is an international organization that provides specialist technical assistance for updating and modernizing tax administrations. The estimated value of this procurement is US$800,000.

Table 1. Thresholds for international bidding and international short lists

Method	ICB works	ICB goods and nonconsulting services	International short list for consulting services
Threshold	US$25 million	US$5 million	US$1 million

Table 2. Main procurement items

Purpose of procurement	Selection method	Estimated date	Estimated amount (US$ million)
Goods and nonconsulting services			
IT equipment (desktop computers, routers, storage facilities)	Pregão Eletrônico	2021-III	2.5
Consulting firms			
Development of the procurement management system	QCBS	2022-II	1.3
Inventory rationalization and reevaluation	QCBS	2021-III	0.8
Process model with development and mapping	QCBS	2023-IV	0.7

C. Procurement supervision

4.6 The ex post supervision method will be used, except where justification is shown for ex ante supervision and direct contracting/single-source selection. Procurements executed using the country system will also be supervised via the country system.

4.7 The supervision method will be determined for each selection process. Ex post reviews will be performed as indicted in the project supervision plan.

Table 3. Threshold for ex post review

Works	Goods	Consulting services
NCB and Shopping	NCB	Less than US$1 million

D. Records and files

4.8 The PCU will be responsible for process documentation and will retain the necessary documentation for supervision and audit purposes.

V. FINANCIAL MANAGEMENT

5.1 **Programming and budget.** SEFAZ/PB is responsible for planning of the PROFISCO II activities, and the PCU for the execution and oversight of the activities, as indicated in the project execution plan and annual work plan. State entities use the following planning instruments: the Multiyear Plan (PPA), the Budget Guidelines Law (LDO), and the Annual Budget Law (LOA). The project budget will be included in the LOA.

5.2 The PCU will ensure that the Bank and local contribution resources for the project are properly budgeted annually and earmarked for execution in accordance with the project programming. The budgetary resources will be recorded as an external source in the year of execution in the Integrated Planning and Budget System (SIOP). The LOA will include the necessary funds for execution of both the external loan and the local contribution.

5.3 **Accounting and information systems.** Public entities in the state of Paraíba work with the Integrated Financial Administration System (SIAF), which encompasses the state's financial, budgetary, and accounting management. The system is auditable and has access profiles and security protocols. It also meets the Bank's requirements on controls and will be used for the execution of PROFISCO II. In PROFISCO I, the financial disbursement and external audit reports required by the Bank were produced in Excel. The project will benefit from the experience of other states that have already implemented a financial management system under PROFISCO II to generate these reports.

5.4 **Disbursements and cash flow.** The project will use the SEFAZ/PB treasury system. Expenditures will be subject to the budgetary and financial execution process and will be duly recorded in SIAF.

5.5 As in PROFISCO I, the Bank resources will be administered through an exclusive account that enables the loan proceeds to be identified and reconciled in terms of both income and payments.

5.6 Disbursements will be made in U.S. dollars in the form of advances of funds, based on a projection of financial needs for up to 180 days. Future advances will be subject to accounting for at least 80% of total funds previously disbursed.

5.7 Expenses considered ineligible by the Bank will be reimbursed from the local contribution or from other funds at the Bank's discretion, depending on the nature of the ineligibility.

5.8 The exchange rate agreed upon with the executing agency to account for expenditures paid from advances of loan funds will be the internalization rate. To determine the equivalence of expenditures charged to the local contribution or reimbursed from the loan proceeds, the agreed exchange rate will be the buying rate set by the Central Bank of Brazil on the effective payment date of the eligible project expenditures.

5.9 **Internal control and audit.** In Paraíba, the CGE/PB is responsible for internal control at the state level, acting through the coordination units for internal control, transparency, internal affairs and integrity, and compliance. It will oversee the project activities.

5.10 **External control and reports.** External control will be exercised by the TCE/PB or by a firm of Bank-eligible external auditors.

5.11 The annual audited financial reports will be delivered pursuant to the terms of reference agreed upon with the Bank within 120 days after the close of each fiscal year.

5.12 **Financial supervision plan.** The financial supervision plan may be altered during project execution in response to evolving risk levels or additional control needs.

Table 4. Supervision plan

Nature and scope	Frequency	Responsibility	
		Bank	Executing agency
Ex post review of disbursements and procurement	Annual	Fiduciary team	PCU – External auditor or TCE/PB
Annual audit	Annual	Fiduciary team	PCU – External auditor or TCE/PB
Review of disbursement requests	Periodic	Fiduciary team	
Supervision visit	Annual	Sector specialist and fiduciary team	

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/20

Brazil. Loan ____/OC-BR to the State of Paraíba. Fiscal Management Modernization Project for the State of Paraíba (PROFISCO II PB). Thirteenth Individual Operation under the Conditional Credit Line for Investment Projects (CCLIP) BR-X1039 - Fiscal Management Modernization Program in Brazil – PROFISCO II

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the State of Paraíba, as borrower, and with the Federative Republic of Brazil, as guarantor, for the purpose of granting the former a financing aimed at cooperating in the execution of the Fiscal Management Modernization Project for the State of Paraíba (PROFISCO II PB), which constitutes the thirteenth individual operation under the Conditional Credit Line for Investment Projects (CCLIP) BR-X1039 - Fiscal Management Modernization Program in Brazil – PROFISCO II, approved by Resolution DE-113/17, on December 8th, 2017. Such financing will be in the amount of up to US$38,412,000, from the resources of the Bank's Ordinary Capital, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on __ ____________ 2020)

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