

INFRASTRUCTURE AND INVESTMENT SECTOR REFORM PROGRAM

(GU-0019)

EXECUTIVE SUMMARY

BORROWER AND GUARANTOR: Republic of Guatemala

EXECUTING AGENCY: The Ministry of Economy (ME), through the program coordination unit (PCU).

AMOUNT AND SOURCE:

IDB quick-disbursing:	US\$100 million (OC)
Technical cooperation:	US\$ 7.65 million (OC)
MIF (grant):	US\$ 1.15 million
Local counterpart funding:	US\$ 2.35 million

FINANCIAL TERMS AND CONDITIONS:

Amortization period:	20 years
Disbursement period:	3 years
Grace period:	66 months
Interest rate:	variable
Inspection and supervision:	1%
Credit fee:	0.75%
Currency:	US\$ (SCF)

OBJECTIVES:

In the telecommunications, electricity and civil aviation sectors the object of the program is to expand coverage, improve the efficiency and quality of service provision, reduce costs connected with service provision and, through recovery of the production costs, ensure sustainable development of these sectors.

The reform proposes achieving these objectives by involving the private sector in service delivery and in financing the expansion of the sectors' installed capacity.

In the hydrocarbons sector, the program proposes to reduce the cost of oil imports and the cost of oil by-products to industry and to the end consumers, through more efficient marketing of hydrocarbons.

The purpose of investment framework reform is to promote competition in the market and to mobilize national and foreign investment by means of a legal framework that eliminates anticompetitive practices and gives the investor legal certainty.

PROPOSED OPERATION: The Bank would support the execution of this program with three instruments: (i) a quick-disbursing loan

associated with infrastructure sector reforms; (ii) reimbursable technical-cooperation funding in the amount of US\$7.65 million to support the implementation of the investment framework and hydrocarbon sector reforms and of the institutional strengthening component in civil aviation (Annex III); and (iii) nonreimbursable technical-cooperation funding in the amount of US\$1.15 million from the Multilateral Investment Fund (MIF) to support the National Airports System (SNA) privatization component (Annex IV). For this funding, the project memorandum (MIF/AT-130) was distributed on May 16 for consideration by the Donors Committee.

The quick-disbursing loan to the Republic of Guatemala, in the amount of US\$100 million from the Bank's ordinary capital, would consist of a first tranche of US\$30 million and three independent tranches totaling US\$70 million to be disbursed in 1997 and 1998, once the relevant reform goals as shown in the sector policy matrix (Annex I) have been achieved.

**PROGRAM
RATIONALE:**

The amount and structure of the quick-disbursing loan are consistent with the structural nature of the sector problems, and with the fiscal and balance of payments needs during the program execution period. The proceeds of the quick-disbursing loan would be used to finance the fiscal and balance of payments impacts resulting from execution of the program of structural reforms (see paragraphs 1.45 to 1.49).

**DESCRIPTION OF
THE PROGRAM:**

In the **infrastructure sectors**, the reforms envisage the adoption of new legal frameworks to: (i) separate the policy-making and regulatory functions from those of financing and direct provision of the services; (ii) establish the regulatory function in specialized, technical agencies; and (iii) reform the regulatory frameworks, eliminating monopolies and opening the sectors up to free competition.

In the **hydrocarbons sector**, the regulatory framework for marketing will be strengthened.

Reform of the **investment framework** will focus on a new legal framework for: (i) providing investors with legal certainty; (ii) strengthening protection for copyright and neighboring rights, patents and trademarks; (iii) establishing legal and administrative mechanisms that grant uniform treatment to national and foreign investors;

(iv) establishing effective and transparent mechanisms for settling disputes; and (v) eliminating anticompetitive and unfair market practices, and protecting consumers.

**ENVIRONMENTAL
CLASSIFICATION:**

The Environment Committee, at its meeting of August 29, 1996, classified this as a Category III operation, and the Committee on Environment and Social Impact (CESI) approved the environmental summary on March 14.

BENEFITS:

In the medium term, the private sector's participation should enable an increase in coverage and efficiency, reduce the treasury's structural deficit, improve the quality of service, and recover costs, including those connected with natural resource protection. The reform of the hydrocarbons sector should make it possible to reduce the costs of importation and domestic fuel prices. Investment framework reform should increase foreign investment flows, technology transfer and the rate of investment.

RISKS:

The chief risks identified are of a political nature and lie mainly in the legal sphere, in the form of the various levels of debate and constitutional challenges regarding the legal instruments and steps of the reform process. The analyses made by the IDB project teams for this operation, and by the World Bank for a parallel technical assistance loan, with legal advice from leading constitutional lawyers, warrant concluding that the strategy adopted by the government is consistent with the Constitution and the country's laws, but as in the past, lawsuits could interfere with the implementation of the reforms.

From the standpoint of the external resources related to privatizations, and to support the peace agreements, there is a risk that if they are not managed strictly as temporary revenues, and no effort is made to increase internal savings, the increase in the supply of foreign exchange could contribute to deferring the need to increase tax revenues, thus endangering external and fiscal sustainability in the more medium term. This risk would be controlled by means of the prospective agreement with the IMF for a macroeconomic and fiscal program that would include identification of specific actions and goals for achieving that objective, and would serve as a basis for evaluating the consistency of the macroeconomic environment with the objectives of the program. If no agreement is reached with the IMF by December 31,

1997, the government and the Bank will agree on criteria for evaluating the macroeconomic environment for program execution, which in principle include: a gradual increase in the tax burden, with a target of 50% over the level recorded in 1995 by the year 2000; repayment of the central government's net external debt; and capitalization of the Central Bank of Guatemala.

In the case of the electricity sector, the privatization of distribution by the Empresa Eléctrica de Guatemala [Electricity Company of Guatemala] (EEGSA) and the startup of the wholesale market are faced with major difficulties in the long-term generation contracts of the "take or pay" type already concluded with the private sector. In the case of the wholesale market, these will represent factors that introduce rigidities, and will reduce the scope and benefits of the reform in the next 10 to 15 years. But in the case of the privatization of EEGSA, the generation costs agreed in these contracts fundamentally impact the financial stability of EEGSA and compromise its privatization prospects. To these risks must be added the lack of autonomy and independence of the National Electrical Energy Commission (CNEE) vis-à-vis the Ministry of Energy and Mines (MEM), as a sector policy agency.

In the case of telecommunications, there is a risk connected with the interest of private strategic investors in participating in GUATEL [Guatemalan Telecommunications Company]. The legislation approved is the most appropriate in light of the technological advances and developments in the telecommunications market, but it excludes incentives which, at the expense of sector efficiency, have been offered in the regulatory frameworks in the recent past in order to attract international operators. Another risk in this sector is connected with the lack of autonomy of the Superintendency of Telecommunications (SIT); however, in view of the nature of the regulatory framework adopted and the limited discretionary authority allowed the regulatory agency, this is a lesser risk (see paragraph 2.16).

In the case of hydrocarbons, the adoption of a legal framework better suited for marketing is an essential prerequisite but not in itself sufficient for resolving the sector's problems. The proposed reform is an important first step, but the problems will not be solved until there is a significant change in the

market structure, which structure is itself essentially due to the oligopolistic structure of the markets and the high degree of vertical integration of the industry worldwide.

**THE BANK'S
COUNTRY AND
SECTOR STRATEGY:**

The Bank's strategy for Guatemala for the 1996-1998 period is to support the government's efforts to achieve four main goals: (i) incorporation of the poor, indigenous and rural population into the sustainable development process; (ii) expansion and improvement of social services; (iii) modernization of the State; and (iv) development and growth of the productive sectors, through promotion of private sector activity in the economy. The proposed operation is focused directly on the last two objectives, and indirectly on social objectives through the release of public sector resources currently earmarked for infrastructure sector financing.

The strategy envisages utilizing a mix of IDB ordinary capital and Multilateral Investment Fund (MIF) and Inter-American Investment Corporation (IIC) resources, and while specifically requiring projects and programs to be technically sound, it also requires that they be simple and easy to execute; compatible with the government's resources; flexible and directly relevant to the country's priorities; and further, that they enjoy clear political support.

**TARGETING OF
LOW-INCOME GROUPS:**

Taking into account that the program benefits are macroeconomic in nature and therefore support the Guatemalan population in general, it cannot be classified as targeting low-income groups or placed in the social equity and poverty reduction category, as specified in Eighth Replenishment document.

**EXCEPTIONS TO
BANK POLICY:**

It is proposed that the direct contracting of UNDP to perform the administrative support activities for the project coordination unit be authorized, together with the contracting of technical-cooperation-related services (see paragraph 3.6 of Annex III).

**SPECIAL
CONTRACTUAL
CONDITIONS:**

The loan contract for the sector loan will contain, in addition to the general contractual conditions for this type of loan, the conditions laid down in the policy matrix (see Annex I).

The loan contract will also include the Bank's standard conditions concerning, *inter alia*, audits, reports, inspections and procurement.

I. FRAME OF REFERENCE

A. Socioeconomic context

- 1.1 Guatemala is one of the poorest countries in Latin America, posting some of the least favorable social indicators of the region. It has approximately 10.3 million inhabitants and an annual population growth rate of 2.9%. Eighty percent of the population lives in poverty and 60% in extreme poverty. The greatest poverty is concentrated in the rural areas and among the indigenous groups (86% and 93% respectively). The indigenous population makes up 42% of the total, one of the highest proportions in the Americas.
- 1.2 During the 1980s, poverty and social conditions worsened markedly. Since 1991 significant efforts have been under way to stabilize the economy; the process has benefited from the support of informal agreements with the International Monetary Fund (IMF). The results obtained in terms of stabilization are considerable, but for them to be consolidated the structural causes of the fiscal and balance of payments imbalances will have to be dealt with. At the same time, adequate attention must also be given to resolving the problems of poverty.
- 1.3 The signature and consolidation of the peace process will require the country to undertake sizable investments and channel resources to accomplish social objectives. According to preliminary estimates, the investments needed just to meet the commitments already made would total over US\$1.6 billion. Financing of these investments will require not only a major domestic effort in order to substantially increase fiscal revenues and change public expenditure priorities, but also the support of the international community.

B. Context of the operation

1. Introduction

- 1.4 The government of President Álvaro Arzú took office in January 1996 and his party gained an absolute majority, 42 of the 80 seats in Congress. This is the third democratically elected government since 1985, after several decades of military governments and a prolonged period of armed conflict in the country.
- 1.5 Reform of the infrastructure sectors and of the framework for investment is a central component of the government's program for 1996-2000. Coverage of the infrastructure sectors is extremely low, and the bulk of the nation's infrastructure is concentrated in Guatemala City. The program recognizes the need to provide employment opportunities and to expand the coverage of the basic services to the population. The sustainability of the process also

requires Guatemala's efficient incorporation into the world economy's globalization process.

- 1.6 In addition to the support of the Bank and of the Multilateral Investment Fund (MIF), this program will also receive technical and financial support from the United States Agency for International Development (USAID) and a Technical Assistance Loan (TAL) from the World Bank (IBRD), which is currently under preparation. The country is also negotiating a stand-by arrangement with the IMF.

2. Macroeconomic context

- 1.7 Since the beginning of the 1990s, Guatemala has been satisfactorily implementing a stabilization and structural adjustment program, the most noteworthy achievement of which has been the adoption of policies designed to improve economic efficiency and competition, such as: (i) decontrolling prices for the great majority of products, with the exception of public utility tariffs; (ii) joining the World Trade Organization (WTO); (iii) cutting duties on imports from outside the Central American Common Market (CACM); (iv) eliminating price control mechanisms and barriers to domestic trade; and (v) eliminating the majority of nontariff barriers.
- 1.8 From the macroeconomic standpoint, in addition to the fiscal and monetary adjustments effected, efforts have also been made to improve coordination among these policies in order to: (i) achieve a balanced budget; (ii) increase the tax burden by means of more efficient use of public funds and greater efficiency in tax collection; (iii) ensure price stability; (iv) establish an exchange rate determined by the market; and (v) reduce interest rates, thereby encouraging saving and private investment.
- 1.9 As a result of these measures, Guatemala's performance since 1991 has been favorable: economic growth has been 4.1% per year, inflation has been held at around 11% per year, and the exchange rate has remained stable, with an upward trend. More recently, coordination between the Ministry of Public Finance (MFP) and the Bank of Guatemala has enabled, on the one hand, a shift in the profile of the government's operations away from high-cost short-term debt and toward less costly medium-term (longer than one year) debt and, on the other, a lessening of unnecessary pressures on the price of money.
- 1.10 However, the economy is vulnerable in some areas. On the external front, international reserves represent a little less than three months of imports and only one fifth of broadly defined money supply (M2). The estimated balance of payments current account deficit for 1996 was 3% of gross domestic product (GDP) and is expected to rise to around 4% of GDP in 1997. This increase would, however, be due to the expenditures connected with consolidation of the peace process, and is an integral part of the macroeconomic

strategy based chiefly on external financing of the investment effort during the transition.

- 1.11 On the domestic front, in addition to curbing inflation and reducing the fiscal deficit, a deeper reduction of interest rates will only be achievable if the cost of intermediation is lowered by means of a lowering of the reserve requirement, and if supplementary revenues are obtained through the sale of State assets (GUATEL), 50% of which are expected to be earmarked for payment of the internal debt. To date, the government's internal borrowing, which exceeds 5% of GDP, has exerted monetary and financial pressures that have limited its capacity to fund the deficit with domestic resources. Finally, the tax burden in 1996 was only 8.5% of GDP, which is insufficient to meet the basic social expenditure and public infrastructure investment needs.
- 1.12 In the next three years, from the macroeconomic viewpoint the government's strategy will seek to resolve certain of the structural problems affecting public finances, and will aim to cover resource needs with bilateral external loans and loans from multilateral agencies, foreign investments associated with privatizations, and the grants provided for consolidating peace. This is a base composed of nonrecurring and temporary resources that is to be used to support the maintaining of the economic stability achieved to date and the implementation of the structural changes, without distortion of the external sector situation. It is accordingly vital that discipline be maintained on the fiscal front, in order to prevent the temporary inflows of foreign exchange from causing appreciation of the real exchange rate and erosion of competitiveness of the tradable-goods sectors.
- 1.13 Particularly important in this respect is the adoption of a macroeconomic-fiscal program designed to permanently increase the savings rate, and especially that of the public sector, through an increase in the tax burden as envisaged in the peace agreements, and in the government's strategy for healthy financing of the increases in social spending. This is a central element in the government's negotiations with the IMF.

3. Program with the IMF

- 1.14 The IMF is prepared to support the Guatemalan authorities' economic program through a stand-by arrangement, and also by performing a catalytic role for disbursements from donors and the multilateral agencies. In this connection, the IMF is currently holding discussions with the Guatemalan authorities in order to arrive at an agreement on the economic program for 1997-1998 that will facilitate implementation of the peace program in a macroeconomic framework consistent with price stability and a viable external situation. The aim is to ensure achievement of sustainable economic growth and reduction of poverty. The program discussion

and design process is being coordinated with the work of the IDB, the World Bank, UNDP and other United Nations specialized agencies.

- 1.15 The amount of the IMF financing will be directly proportional to the strength of the program, the main component of which will be strengthening of the public sector's financial position, in particular the level of savings, with the aim of enabling a higher level of public investment and social spending while at the same time reducing the effect of the adjustment on monetary policy. This would lead to improving financial intermediation and creating favorable conditions for investment, private savings and economic growth.
- 1.16 To successfully strengthen the public sector's financial position it is essential to increase the tax burden, which is currently one of the lowest in Latin America. This will make it possible to maintain an appropriate level of investment in the medium term, once external financial assistance reverts to normal levels, thus preserving macroeconomic stability. In this respect, the program will aim to bring about a gradual increase in the tax burden by the year 2000 of the four percentage points of GDP specified in the peace agreements. The program will also include the replacement of nonproductive expenditure with social expenditure and the possibility of introducing cost-recovery arrangements in certain services such as education and health. The program will also include adjustments required in the prices and tariffs of public goods and services.
- 1.17 In addition to the fiscal effort, the program will also include monetary policy actions and structural reforms. Regarding monetary policy, it is important that the reserve requirements be standardized and reduced so as to lessen the distortions in the financial market that currently limit monetary control, weaken the financial institutions and foster financial disintermediation. Approval of the amendments to the Central Bank law that will permit application of the reserve requirement to all liabilities similar to deposits and reduction of the requirement would help achieve this objective. In order to prevent additional demand pressures resulting from the lowering of the reserve requirement, and should it be necessary, the program calls for the use of Bank of Guatemala market instruments to neutralize liquidity until the fiscal effort is consolidated. In addition, the program will include careful management of internal debt repayment (both that of the Central Bank and of the government) to limit inflationary pressures that might be generated by the monetization involved.
- 1.18 The prospective agreement with the IMF will be used as a basis for evaluating the macroeconomic environment for the program. If no agreement is reached with the IMF by December 31, 1997, the government and the Bank will agree on criteria for evaluating the macroeconomic environment during program execution, including: a gradual increase in the tax burden, with a target of 50% over the

level recorded in 1995 by the year 2000; repayment of the central government's net internal debt; and capitalization of the Central Bank of Guatemala.

4. Legal context

- 1.19 To be able to implement the reforms envisaged in the program, the General Electricity Law, the General Telecommunications Law and an amendment to the contracts and concessions legislation [*Ley de Contrataciones*] (Decree 57-92) have been approved. Also, with the aim of encouraging or enabling private sector participation, bills have been prepared on the aviation sector and the investment framework to promote foreign investment and strengthen protection for copyright, patents and trademarks and consumer protection and to foster competition.
- 1.20 These reforms have been possible because the party in government has an absolute majority in Congress. Nevertheless, there are certain risks of a legal nature that derive in large measure from the fact that some of the changes affect agencies that were created by approval of a qualified majority in Congress; this applies especially in the case of the Empresa Guatemalteca de Telecomunicaciones [Guatemalan Telecommunications Company] (GUATEL) and of the Instituto Nacional de Electrificación [National Electricity Authority] (INDE). Mainly, it has been suggested that a qualified majority may be necessary for approval of any amendment to the GUATEL and INDE laws. It has also been suggested that the effect of the above-mentioned reforms are equivalent to the elimination of autonomous agencies, for which a qualified majority is also required.
- 1.21 The General Electricity Law had the effect of eliminating any regulatory function that INDE had. It also clearly established a free-market policy, ordering the segregation of transmission, generation and distribution activities. In fact, the law eliminated INDE's role as arbiter and party in the sector, together with the natural monopoly it enjoyed under the previous system. Similarly, the General Telecommunications Law did away with the regulatory function assigned to GUATEL, eliminating its role as arbiter and party in the sector and the monopoly specifically assigned to it under the previous system. Finally, the amendment of the contracts and concessions legislation complements the amendments already described, expanding the definition of property and assets to include the concept of *block assets*, which allows state agencies to conclude contracts for an array of movable property and real estate, including intangible assets. This means that an institution can dispose of a set of assets and liabilities together with legal, contractual or other relations such as good will, use of transmission bands, etc.
- 1.22 Notwithstanding these objections, separately and independently the Bank and IBRD project teams, with the support of Guatemalan legal

advisers, believe that the government's legal strategy for implementing the proposed changes is consistent with Guatemala's Constitution and legislation, and that the laws and legal amendments approved will make it possible to implement the desired reforms without requiring approval by a two-thirds majority in Congress.

- 1.23 The analysis reflects that the GUATEL and INDE laws were approved by a qualified majority in Congress exclusively so that they could be granted autonomy. The proposed reforms will modify these institutions' objectives, thereby affecting the respective sectors but without limiting their autonomy within the sector framework. Provided the reforms respect this autonomy, there is no obstacle to reforming the electricity and telecommunications sectors by means of legislation approved by an absolute majority in Congress. The respective legal reports prepared for the IDB and IBRD by constitutional lawyers in Guatemala are available for consultation in the project's technical files.
- 1.24 The strategy adopted does, however, entail the risk, which has already materialized in the case of the electricity, telecommunications and contracts and concessions laws, that the legality of the reforms may be contested. The fact that an appeal is filed does not mean that it will be granted or that the law will be declared void or provisionally suspended, but it could hold up enforcement of the law. In point of fact, the Constitutional Court decided not to suspend the above-mentioned laws while it considers the merits of each case. It should be noted that this risk is not unique to this program, since in Guatemala the judicial system is frequently used to block the implementation of reforms.

C. Main problems

1. Problems in the infrastructure sectors

- 1.25 The main problem in these sectors is the imbalance between the supply of and demand for resources to be able to operate efficiently and finance the expansion of capacity in the electricity, telecommunications and civil aviation sectors.

To resolve the shortcomings in provision of services and meet the growth in demand in the next five years in the civil aviation, telecommunications and electricity sectors, Guatemala needs around US\$2.2 billion. This represents an annual investment of approximately 5% of GDP.

a. Civil aviation sector

- 1.26 The sector lacks the resources and institutional framework necessary to provide adequate service. Its resource base does not allow acceptable minimum levels of maintenance of equipment or

facilities to be reached and is insufficient for renewal of equipment and incorporation of technological advances related to the standards of service required worldwide. Moreover the minimum levels of efficiency and safety as laid down in the recommendations issued by the International Civil Aviation Organization (ICAO) are compromised. The United States Federal Aviation Administration (FAA) has currently made entry of Guatemalan carriers into that country conditional upon implementation of corrective measures by the regulatory authorities, which they have not yet been able to do.

- 1.27 The sector is governed by the Civil Aviation Law of 1949. The General Directorate of Civil Aeronautics (DGAC) administers the airport and navigation support infrastructure, and also performs all aspects of technical inspection. The DGAC lacks the financial, operating, and administrative autonomy to perform these functions. Around 90% of the sector's revenues are transferred to the central government.

The investment needs connected with the modernization and expansion of Guatemala City's La Aurora Airport and of the country's other main airports in order to reach reasonable safety and efficiency standards amount to US\$150 million. These requirements will be substantially greater if recommendations are accepted to relocate the Guatemala City airport in order to comply with internationally accepted safety standards.

b. Telecommunications sector

- 1.28 In Guatemala all telecommunications services are provided by the State-owned enterprise GUATEL. GUATEL currently has to operate within an institutional framework that does not give it the management flexibility, financial and operating autonomy or incentives necessary to respond adequately to the challenges represented by the globalization of the economy and the development needs of the information economy.

The program to expand and modernize telecommunications services over the next five years will cost around US\$1.2 billion. To achieve acceptable coverage and efficiency goals, GUATEL must have timely access to modern technologies and to financing and the capacity to execute investments of at least US\$240 million per year.

- 1.29 The sector has the usual characteristics associated with the model of a State-owned enterprise providing services under monopoly conditions, namely: high unmet demand - GUATEL has 400,000 connections while there are requests for 800,000 lines; low coverage, only 3.6 lines for every 100 inhabitants; low reliability and

service quality, with a call completion rate of only 37%; distorted tariffs, with international long-distance service subsidizing local service; diversion of resources to finance the rest of the public sector; and overstaffing for present service levels, with five times the number of employees that efficient enterprises have.

c. Electricity sector

- 1.30 The bulk of electricity consumption in Guatemala is concentrated in the environs of Guatemala City, with 76% being sold in Guatemala City and in the departments of Escuintla and Sacatepeque. Together with this concentration, coverage levels are only at 41% while per capita electricity consumption is only 250 kWh, one of the world's lowest.
- 1.31 The Ministry of Energy and Mines (MEM), created in 1983, is the sector's apex organization and is responsible for policy-making and for coordination with the other sectors of the economy. The main sector enterprises are INDE, the Empresa Eléctrica de Guatemala [Electricity Company of Guatemala] (EEGSA), the Empresas Eléctricas Municipales [municipal electric companies] (EEMs) and, as of recently, the Empresas Eléctricas Privadas [private electric companies] (EEPs), which are generators only. INDE is responsible for the coordination of the National Interconnected System (SNI), and for the bulk of hydroelectric generation and a part of the thermal generation system and for distribution outside the metropolitan area. EEGSA operates as a distribution enterprise although it also has generation capacity, and serves the metropolitan area, which represents around 75% of the country's electricity market. Both INDE and EEGSA are State-owned enterprises, although the latter is governed by the commercial code applicable to any corporation.
- 1.32 The MEM does not have the structure, capacity or resources to perform its functions adequately; its normative, regulatory and business roles are confused and mixed together and there is political interference in its business and regulatory decisions, especially in the regulatory function of tariff setting and approval. The foregoing is also reflected in the overstaffing of the two enterprises and in the shortage of qualified personnel.
- 1.33 The system has not been adequately maintained and has been allowed to deteriorate, especially the transmission facilities; it is overloaded and unreliable. Some equipment in operation has exceeded its normal useful life. The tariffs paid by consumers have been kept below the production costs and, without the reform measures, both INDE and EEGSA would be embarking on a process of rapid financial deterioration. A large part of EEGSA's losses are the result of contracts with private operators under which the contracted purchase tariffs for generation are higher than the tariffs charged to consumers.

- 1.34 INDE, within the framework of Government Resolution 4-93, 1/ has signed take or pay contracts with 12 private generators for a total of 187 MW. All this capacity is scheduled to enter the system before 1998 which, combined with the commitments of the same type assumed by EEGSA, means that a significant proportion is subject to an obligation to purchase on the part of the public enterprises (INDE and EEGSA).
- 1.35 The long-term (majority 15 years) commitments to purchase capacity and energy assumed through these contracts define a starting point that will limit competition for some time and affect the distribution privatization process.

The growth projections involving electric energy demand for the next 10 years, of around 6.5% per year, will require investments of US\$1.65 billion, i.e. an annual average of US\$165 million. The main component (75%) is represented by additional generation facilities, which are expected to be executed by private investment.

2. Problems in the hydrocarbons sector

- 1.36 Guatemala produces some 18,000 b/d of heavy crude for export. Decree Law 109-83 and its main regulations of 1983/84 still constitute the legal framework for hydrocarbon exploration and production in Guatemala. In recent years the international oil industry has shown little interest in the areas offered for exploration in the country. The legislation and the contractual conditions are antiquated and not competitive at world level.
- 1.37 Consumption of petroleum by-products has increased considerably in recent years and the value of hydrocarbon imports has reached around 12.5% of the foreign exchange generated by goods exports.
- 1.38 Until 1992 Guatemala was a typical case of regulation and control of the marketing chain. The State held the import monopoly, the refinery operated with guaranteed profits, and the distributors, transporters and retailers had controlled margins and prices. Despite the fact that as of 1992 the import monopoly was eliminated while prices and margins for the majority of products were decontrolled as of 1994, the lack of adequate conditions for the operation of a competitive market has prevented the reforms from being reflected in significant changes in the structure and levels of prices. Application of the system is voluntary and, in

1/ Government Resolution 4-93, approved in February 1993, authorized INDE to enter into contracts to purchase electrical power and energy directly, without having to fulfill quotation and bidding requirements normally required, from individuals or corporations in a position to sell energy and power needed by the country.

practice, price calculations are based on prices that are substantially higher than the Gulf Coast prices (Caribbean postings) set by the transnational companies that dominate the market.

- 1.39 The structure of the market is characterized by the presence of a small number of companies that own the existing infrastructure. The refinery, owned by a foreign oil company, is operating under a concession contract that expires in 2002 and grants it, among other benefits, a 10% protective tariff on imported by-products in favor of crude imported by the refinery. Another two international companies operate small import terminals and, together with the refinery, control the marketing system of all products except for liquefied gas.
- 1.40 The oligopolistic structure of the market, the absence of a modern legal framework and the presence of an inflexible State bureaucracy are factors that have prevented the deregulation measures from attracting new participants into the supply chain. It is estimated that this lack of competition represents an additional cost of around US\$40 million to Guatemalan consumers.
- 1.41 Accordingly, in addition to a modern legal framework, reform of the sector will require a regulatory and institutional structure that increases efficiency through promotion of competition, which in turn requires markets without dominant companies and without barriers to entry. Recently, at least two groups of national and international companies have expressed interest in setting up independent import terminals and offering their services to any importer and/or consumer on competitive terms.

3. Problems of the investment environment

- 1.42 From this viewpoint, the program's raison d'être lies in the lack of growth in private investment resulting from legal, institutional and statistical frameworks unsuited to the requirements of the new conditions prevailing in the world and national economies.
- 1.43 National legislation: (i) in the case of intellectual property, is either nonexistent or too outdated to be of any use in the new arrangements connected with the globalization of the world economy and technological advances; (ii) in the case of foreign investment, is scattered among different bodies of law, introduces uncertainty and increases transaction costs; (iii) in the case of consumer protection and competition, does not offer consumers and producers proper protection, nor does it curb anticompetitive practices.

D. Proposed operation

- 1.44 The operation consists in a quick-disbursing loan to the Republic of Guatemala of US\$100 million from the Bank's ordinary capital, to be disbursed in a first tranche of US\$30 million plus three

independent tranches totaling US\$70 million to be disbursed in 1997 and 1998 once the reform goals shown in the sector policy matrix (Annex I) have been accomplished. The loan would have a disbursement period of 36 months.

- 1.45 To support investment sector reform, the operation also includes (see Annex III) a proposal for approval of reimbursable technical-cooperation funding of US\$7.65 million from the Bank's ordinary capital, and nonreimbursable technical-cooperation funding of US\$1.15 million from the MIF (Window I, Technical Cooperation Facility) to support the inclusion of the private sector in civil aviation (see Annex IV).

E. Rationale for the sector loan

- 1.46 The structural nature of the problems to be resolved and the type of financing proposed are consistent with the program adopted and with the fiscal and balance of payments needs resulting from the reforms. Proposed structural reforms will have a positive fiscal impact; however, during the execution of the program, at the same time as the government has to step up spending in the social sectors to meet the commitments connected with the agreements for consolidating peace, from the strict standpoint of the public finance cash position the program will have an unfavorable impact on the central government's revenues during the execution period.
- 1.47 From the revenue standpoint, the proposed reforms will put an end to the resource transfers from GUATEL and the DGAC to the central government, while from the expenditure side resource needs will increase for meeting the labor-related liabilities connected with the reform and privatization of the public enterprises.
- 1.48 The above fiscal impacts and pressures, which are usual in this type of program, will not necessarily be mitigated by external resource inflows similar to those observed in other privatization programs in the region. This is because in defining the reform program the government made the efficiency and competition objectives paramount and the privatizations do not include the revenue incentives associated with exclusive operating rights. The value of the concessions will also probably be affected by the investment commitments which will be required of the possible investors.
- 1.49 Moreover, and for reasons already noted that are related to the macroeconomic program, the government will use around 50% of the resources obtained from the privatizations for reducing the domestic debt, by means of which it could save around US\$150 million in interest. In parallel, the remaining balance of the revenue from the privatizations will be used to help fund the expenditures connected with consolidation of the peace program. Should these resources fail to materialize, if Guatemala has to finance these expenditures with

external credit, the interest it would have to pay is estimated at around US\$140 million.

- 1.50 For these reasons, the proposed Bank financing is an essential component of the external support needed to make the structural reforms viable. Moreover, the fiscal and balance of payments benefits justify the proposed financing arrangements.

F. Outcome of the program and development impacts

- 1.51 It is expected that the private sector's participation will make it possible to reduce the fiscal burden, increase coverage and improve the quality of service delivery, and recover costs, including those connected with the activities designed to protect natural resources. The aim of the hydrocarbons sector reform is to reduce the cost of importing fuels and lower domestic prices. The reform of the investment framework is intended to increase foreign investment flows, technology transfer and the rate of investment.

G. Lessons learned

- 1.52 Probably the most important lesson taken into account in designing the operation is related to the ownership of the reform program combined with the necessity that the Executive Branch have the capacity and be in a position to give direction and assume the costs connected with implementation of the program. In this respect, during the preparation of the program the Bank made sure that the proposed reforms are an integral part of the government's program and that their strategy and scope are the most suited for the time and for the country's current circumstances. This has been particularly important for selection of the sectors and the scope of the reforms in each of them. The Bank's work has focused on providing the technical support needed for designing the program, ensuring its internal consistency and rendering its implementation viable.
- 1.53 Regarding the design of the operation, and based on previous experience with reforms involving a plurality of independent sectors in which the reforms will be implemented at their own pace, the tracking and monitoring of the program and the structure of the disbursements have been designed around a simple and flexible policy matrix with floating tranches, and emphasis has been placed on the end results and on benchmarks that provide a measure of security concerning the irreversibility of the program's progress.
- 1.54 With regard to the execution of the program, experience shows there are two areas that require special attention: (i) one is the lack of national experience for administering and managing resources in programs as complex as this, together with the complexity of the national legislation on the contracting of consultants; (ii) the other is related to the institutional weakness of the State agencies for implementing programs of this sort. In this

connection, the salary scales and budgetary constraints are obstacles to retaining qualified human resources and to ensuring availability of adequate equipment and materials. To resolve the first of these problems the execution plan includes participation by the United Nations Development Programme (UNDP), while to address the second concern an executing unit will be created that will be financed with counterpart resources and the proceeds of the program's technical cooperation loan.

II. SECTOR REFORM PROGRAM

- 2.1 The purpose of the reform of the telecommunications, electricity and civil aviation sectors is to expand coverage, increase efficiency and upgrade the quality of service delivery, reduce the costs connected with delivery, and by means of recovery of production costs, ensure the sustainable development of these sectors. The aim of investment sector reform is to develop and strengthen free competition, eliminate market monopolies and promote private investment.
- 2.2 In the *infrastructure sectors* the reforms provide for adoption of a new legal framework for: (i) reforming the regulatory frameworks, eliminating monopolies and opening the sectors up to free competition; (ii) separating the policy-making and formulation, regulatory and direct service provision functions; (iii) establishing the regulatory function in small, specialized, autonomous and independent technical agencies; and (iv) involving the private sector in the financing, expansion and direct provision of services. In the *hydrocarbons sector* the regulatory framework for marketing will be strengthened.
- 2.3 Reform of the *investment framework* provides for adoption of a legal framework in order to: (i) give investors legal certainty; (ii) strengthen protection for copyright and neighboring rights, patents and trademarks; (iii) establish legal and administrative mechanisms that will give uniform treatment to national and foreign investors; (iv) establish flexible and transparent mechanisms for resolving disputes; and (v) eliminate unfair market practices and protect consumers. 2/
- A. Civil aviation sector
1. Objectives of the subprogram
- 2.4 To resolve the civil aviation sector's structural problems, the reform aims at: (i) transferring the operation, development and financing of the expansion of the air transportation infrastructure capacity to the private sector; and (ii) strengthening the DGAC to enable it to efficiently perform its policy-making and regulatory responsibilities.
- 2.5 The main goals of the strategy are the following:
- a. Reform of the institutional and legal framework in order to redefine the roles of the public and private sectors, establish

2/ The policy elements and the scope of the investment sector reform program are included in Annex III and in Appendix 1 to that annex.

the competence of the new Civil Aviation Directorate (DAC) to reform the regulatory framework, and open the sector up to private participation in the provision of airport and air navigation services.

- b. **Institutional strengthening of the DGAC** to enable it to properly perform its technical and economic regulatory functions. This element of the strategy calls for the complete restructuring of the present DGAC, together with updating and automation of its practices and procedures (in accordance with ICAO standards) ^{3/} and institution of management information systems and appropriate training in this area. The training will also include strengthening of the environmental inspection and monitoring capacity of the DGAC.
- c. **Private Sector involvement.** (i) **Airports.** The strategy proposes granting concessions to the private sector, as they now stand, for the operation, development, maintenance and management of La Aurora Airport and, if feasible, San José and Santa Elena Airports. If the technical and financial analysis concludes that it is feasible, the maintenance and development of the rest of the airports in the system (i.e., small landing strips and secondary airports) would be financed by means of the concession fee paid by the concession holder for the three main airports. This fee would be used to set up an airport development fund to cover the maintenance and operating costs of the rest of the system (less than 2.5% of total movement in the system). (ii) **Air traffic control.** The strategy also calls for exploring the possibility of transferring the responsibilities for financing, expansion and operation of the air traffic control services to the private sector. However, unlike the airports, Guatemalan air navigation services may very well not generate sufficient revenue flows to cover capital costs (i.e., procurement and financing of equipment) after operating costs are met.

2. Policy elements of the subprogram

- 2.6 The proposed bill establishes a new regulatory framework that is based on principles such as: fostering of competition, promotion of efficiency by means of market mechanisms, opening of the market in support of an open-skies policy and minimization of regulatory discretionary authority, and defining of the State's sphere of

^{3/} The review and updating of the administrative and control processes, to ensure application of the rules and regulations resulting from the standardization required by ICAO. Adoption of the internationally accepted standards laid down in the 18 ICAO annexes. The establishment of communication and updating mechanisms with the international agencies.

action with respect to air transportation, airports and airfields, navigation services and air traffic control.

- 2.7 The project recognizes that the sector's efficiency can be increased by fostering and promoting competition, for which reason regulation is minimized. The bill accordingly establishes the principle of "freedom of competition" regarding the provision of the services connected with aeronautical activities, together with the primacy that will be assigned to free negotiation of the charges and tariffs for the services covered by the law. In the event that free negotiation fails, the bill establishes efficient arbitration mechanisms for settling disputes, which are described therein.

3. Plan of action for the reform and status of the subprogram

- 2.8 The action plan for the privatization component includes the following activities: (i) send the new legal framework to Congress for approval; (ii) prepare a long-term concession for transferring the operation, management and development of La Aurora Airport and, depending on the findings of the technical evaluations included in the program, the concession of other airports in the country.
- 2.9 The possible concession includes all activities (aeronautical and commercial) from the moment that the aircraft reaches the terminal (embarkation pier, access gate or tunnel) to the moment that the aircraft with passengers/freight on board leaves the terminal, and investment commitments by the license-holder for developing the airport infrastructure and meeting increases in demand on the basis of the appropriate international standards. Moreover, the concession requires the presence of an international airport operator, and would be granted by means of an international competitive bidding process. In addition, the feasibility and mechanisms for making concession of air traffic control services to the private sector a viable proposition will be explored.
- 2.10 The action plan for institutional strengthening of the DGAC includes reorganization of the DGAC to adapt it to the new legal framework, the development of technical rules and standards compatible with the international standards, strengthening of the capacity to inspect and monitor the environmental aspects of the concessions, and equipment and training for the DGAC. To date, with the Bank's assistance the bill has already been prepared and the draft versions of the invitations and terms of reference for the consulting services on involving the private sector have been agreed with the Bank (see Annex III).
- 2.11 For execution of this subprogram, proposed support from a MIF grant of US\$1.15 million is anticipated, together with US\$1.8 million from the technical assistance loan and US\$900,000 from the

counterpart funds to be furnished by the Ministry of Communications, Transportation and Public Works (MCTOP) and the DGAC.

- 2.12 Disbursement of the quick-disbursing loan resources are conditional on achievement of two of the program's direct objectives. The first objective is approval of a Civil Aviation Law (one of the conditions precedent to disbursement of the first tranche) in terms essentially similar to those contained in the draft version already agreed with the Bank. The second, which applies specifically to approval for disbursement of US\$25 million from one of the three floating tranches, is completion of the subprogram for involvement of the private sector (see Annex I: Sector policy matrix). It is expected that that action will be completed by the end of the first half of 1998.

B. Telecommunications sector

1. Objectives of the subprogram

- 2.13 The purpose of the telecommunications sector reform is to increase the coverage and reduce the cost of telecommunications in Guatemala, to transfer the responsibilities for financing, expanding and providing telecommunications services to the private sector, and to reduce public sector participation exclusively to policy-making and regulatory functions.

2. Policy elements of the subprograms

- 2.14 The key sector policy elements include: demonopolization of telecommunications; sale of a majority interest in GUATEL to a private operator; and liberalization for efficient allocation of the radio spectrum. Telecommunications regulation remains the responsibility of the Superintendency of Telecommunications (SIT), which was recently created by law and is charged with ensuring the interconnection of the public networks and unbundling of the network. In addition, a Fund for the Development of Telephony (FDT) will be established to expand coverage in the rural areas.
- 2.15 The program is based on Decree-Law 94-96, General Telecommunications Law, promulgated by the Executive Branch on November 18, 1996, plus amendments to the current legislation concerning sale and transfer of State property in the State Contracts and Concessions Law.
- 2.16 The General Telecommunications Law establishes a regulatory framework that is based on integration of telecommunications and information technology, and on the technological changes that have drastically reduced the barriers to operating in the sector. The law accordingly establishes free competition in the market and reduces the scope of regulation to access to essential resources. The prices and conditions for access to essential resources will be

negotiated between the parties. If agreement cannot be reached, the conflict will be resolved by the SIT. The law reduces the regulatory agency's discretionary authority to a minimum and explicitly establishes long-term average incremental costs for calculation of the access charges that the SIT will use for determining the respective charges.

- 2.17 Lastly, the law stipulates creation of the FDT for promoting the development of telephone service in rural and/or low-income urban areas. The fund will be capitalized with resources from the fees for permits to use the radio spectrum, the interest generated by said funds, government transfers and grants from other organizations.
- 2.18 Regarding the radio spectrum, the law introduces a framework based on the market for its allocation, limiting the SIT's role to following procedures that are clearly laid down in the law. The law establishes usufruct rights that will be granted by means of auctioning permits that will function as transferable and negotiable instruments. These permits will not be restricted to a particular use or technology; they will be granted for 15 years, will be renewable, and will be transferable by sale or lease.
- 2.19 The most important distinctive elements of this strategy compared with other experiments in this sector are: (i) the objective of sector efficiency and development has been made paramount with the adoption of a system favoring competition and **without an exclusive right period** initially; and (ii) as a result of the foregoing, the reform requires and includes the **total rebalancing of telecommunications rates** as a condition precedent to the opening of the sector to free competition.

3. Plan of action for reform and status of the subprogram

- 2.20 In the context of the new Telecommunications Law, GUATEL has already adjusted its international long-distance and local service rates prior to network interconnection and access to essential resources being made obligatory.
- 2.21 Together with promulgation of the law, the SIT has entered into operation, the superintendent has been appointed, and the transfer of MFP resources to the SIT to fund the latter's operation in its first year has been approved.
- 2.22 As part of the GUATEL privatization component, the investment bank has already been retained. With the rebalancing of tariffs the cross subsidies have been eliminated and the future expansion of local telephone service will be based entirely on the local service rates. The purpose of the privatization is to bring in a strategic operator to control the enterprise's operation, but the government

has not yet made a decision on the best market strategy for selling GUATEL stock. GUATEL's workers would retain a 5% stake in GUATEL.

- 2.23 The disbursement of the proceeds of the quick-disbursing loan will be tied to two important program objectives. The first is approval of a General Telecommunications Law (one of the conditions for presentation to the Board). The second, for approval of disbursement of US\$20 million from one of the three proposed floating tranches, is completion of the GUATEL privatization subprogram (see Annex I: Sector policy matrix). In accordance with the timetable, the privatization would take place in the third quarter of 1997, and the resources of the financing connected with reform of this sector could be disbursed in the second half of 1997.
- 2.24 Up to this point the government has been receiving technical and financial support from USAID, but has mainly used GUATEL's own resources for the preparation and execution of various components of this program, including preparation of the General Telecommunications Law, recording of requests for use of the spectrum, and the operating budget of the SIT for 1997. Execution of the actions pending under this subprogram will be funded with US\$2.96 million from the World Bank TAL.

C. Electricity Sector

1. Objectives of the subprogram

- 2.25 The reform of the power industry is intended to expand coverage and increase efficiency in the provision of the services by replacing today's vertically and horizontally integrated monopolies with free and competitive electricity markets, and through the involvement of the private sector in the financing, expansion and direct provision of the services.
- 2.26 The proposed reform is consistent with the objectives and components of the Central American Electric Interconnection System (SIEPAC) project inasmuch as, in addition to the vertical unbundling of the various activities (generation, transmission, distribution), it provides for enabling consumers (distribution from large-scale consumers) to opt for acquiring their supply from generators outside the country. Nevertheless, as in other countries, it will be necessary to carry the reform process further in order to avoid cross ownership and ensure the autonomy of the regulatory agency.

2. Policy elements of the subprogram

- 2.27 The program is based on Decree-Law 93-96, General Electricity Law, promulgated by the Executive Branch on November 15, 1996, and on the amendments recently approved by Congress to the current

legislation on sale and transfer of State-owned property in the State Contracts and Concessions Law.

- 2.28 The new legal framework establishes the separation of the policy-making and regulatory functions, which will be retained by the State, from those of financing and direct provision of the services, which in principle will be transferred to the private sector. Policy-making and formulation are a direct responsibility of the Ministry of Energy and Mines (MEM).
- 2.29 Regarding the regulatory function, the government was unable to obtain the necessary support in Congress (qualified majority) to approve creation of an autonomous and independent institution, which would have been the most desirable route. The General Electricity Law accordingly had to be limited to establishing a regulatory body, the National Electrical Energy Commission (CNEE), as an agency attached to the MEM and having its own financing (0.3% of regulated enterprises' billing). In accordance with the government's policy objectives, the CNEE will have the autonomy and independence to perform its function, but it is clear that this is a temporary alternative pending a political situation that will enable creation of an autonomous and independent CNEE.
- 2.30 The law establishes the vertical unbundling of the generation, transmission and distribution activities, the decontrolling of prices for energy sales to distributors and large-scale consumers in the wholesale market, the creation of an hourly energy market, free access to the transmission and distribution systems, and establishment of a rate policy that regulates the transmission and distribution activities separately on the basis of efficiency criteria.
- 2.31 The rates charged to ultimate customers in the power and energy components will be calculated by the CNEE as the sum of the weighted price of all the distributor's purchases referred to the entry of the distribution network and the distribution value added. In turn, the General Electricity Law provides that purchases of electricity by the distributors of final distribution service will be made through public bidding and the public will have access to all the information relating to the bidding and award process.
- 2.32 The starting up of the wholesale market is essential to the success of the program. The basic foundation of the reform is the replacement of horizontally- and vertically-integrated enterprises with an **electricity market** in which generators, distribution enterprises and large-scale consumers freely contract for energy. The bill establishes a market with two types of transactions: freely negotiated long-term contracts, and others for short-term transactions designed to reconcile differences between energy transfers in actual operation and the contracted values.

- 2.33 Effective and efficient operation of this wholesale market, a central element of the reform, requires unbundling of the generation, transmission and distribution activities, and also separation of ownership in these activities, which is currently totally in the hands of the State. The law approved does not prohibit cross ownership, and only requires separation of enterprises.
- 2.34 The reform is therefore based on the one hand on the vertical unbundling of generation, transmission and distribution activities in INDE, and on the other, on the privatization of INDE's and EEGSA's distribution activities. The prices that emerge from the operation of this market will determine the incentives for efficiency in allocation and expansion of the electricity system.
- 2.35 The reform process will have a lengthy maturation period. The transformation of INDE and the privatization of EEGSA's distribution activity are central aspects of the reform which serve as the basis for justifying the specific goals and conditions for disbursement of this operation's resources.
- 2.36 In parallel with these activities, in order to increase the probability of success of the program, steps will be taken to: (i) strengthen the CNEE and train its staff; (ii) rationalize the rates and reorganize EEGSA's and INDE's finances; (iii) appropriately deal with the transfer of existing private generation contracts to the future market agents; and (iv) overhaul the transmission and subtransmission systems, which are in a serious state of disrepair.

3. Action plan for reform and status of the subprogram

- 2.37 In addition to approval of the changes in the legal framework and preparation of the regulations of the General Electricity Law (general regulations, technical standards, and the regulations for the wholesale market), the government has taken important steps to move the reforms forward. Specifically, with the assistance of USAID and the IBRD, progress has been made with the sale of EEGSA's generating facilities and execution of the action plan for unbundling the generation, transmission and distribution activities in INDE, while EEGSA has already begun implementation of the distribution rate adjustment.
- 2.38 Two of these actions are particularly critical for ensuring the success of the program. One is the need to move forward with the transfer of EEGSA's contracts with private generators, which is a matter that will be taken care of during the preparation of the terms of the privatization of EEGSA's distribution business, and the other is the question of EEGSA's distribution rates.

- 2.39 Regarding rates, execution has already been started of the program to adjust EEGSA's electricity rates by 27% and INDE's by 22%. With this adjustment, EEGSA's rates will be at a level equivalent to 97% of the economic rate and those of INDE at 95%. The new rates should enable EEGSA to totally eliminate the financial losses projected for the 1997 budget year. To date, the adjustment already put into effect in the first quarter of 1997 has reduced the financial losses by 52%.
- 2.40 The resources from the quick-disbursing loan are tied as follows to the program objectives: the first tranche, with approval of a General Electricity Law and adjustment of the electricity distribution rate (one of the conditions for presentation to the Board). The disbursement of US\$25 million from one of the proposed three floating tranches will be made once the vertical and horizontal unbundling of INDE's and EEGSA's business activities has been completed, EEGSA's distribution business has been privatized (see Annex I: Sector policy matrix) and the wholesale market administrator is in operation. According to the timetable, this tranche would probably be disbursed in the first half of 1999.
- 2.41 The execution of the reform program, and in particular the steps and actions described above, will be financed with US\$5.5 million from the World Bank's TAL, plus additional funding from USAID for the divestiture of EEGSA's generation facilities.

D. Hydrocarbons sector

1. Objectives of the subprogram

- 2.42 The purpose of the program is to promote development of a free and competitive market that will ensure efficient supply of petroleum products in a manner compatible with protection of the environment. The reform program includes legislative and regulatory measures, institutional strengthening and improved management of the MEM's General Directorate of Hydrocarbons (DGH), in its capacity as oversight and inspection agency, and as promoter and single window for investors.

2. Policy elements of the subprogram

- 2.43 With support from the Bank, the government has developed a *draft Marketing Law* designed to establish a framework for promoting free competition, facilitating the granting of licenses to participate in the various activities of the hydrocarbons supply chain, clearly defining the responsibilities of the State, removing the barriers to entry by new operators, and establishing parameters for ensuring and controlling the quality of the products. The plan is to limit the State's role to the granting of licenses to private operators and to monitoring and supervision of the activities. The adoption of a legal framework that groups together all provisions connected with marketing is justified by the need to empower the State

agencies charged with regulating and punishing anticompetitive behavior, and to organize the numerous pertinent provisions that are scattered among a variety of laws and regulations.

3. Plan of action for the reform and status of the subprogram

- 2.44 The institutional strengthening seeks to eliminate the bureaucratic obstacles for participants and new investors in the supply chain and to modernize the management of the regulatory body for the subsector. The program includes strengthening of the DGH's management capacity, the organization of the exploration and production databank, development of staff training programs, and modernization of the equipment.
- 2.45 Specific environmental regulations for the subsector will be prepared in order to resolve current problems with the exploration and production areas and to remedy the lack of regulation for the marketing of petroleum products. The technical cooperation operation includes the support necessary for formulating an environmental strategy and the environmental regulations.
- 2.46 The problem of lack of interest displayed by highly reputable international companies with the capacity to participate in exploration in the country will begin to be resolved with support from the technical cooperation operation. The government intends to prepare a strategy for promoting investments in exploration of areas offered to international companies, with an institutional structure that can respond efficiently and effectively to the dynamics of the sector by means of a single-window arrangement.
- 2.47 To strengthen the government's inspection and planning functions, the DGH will be given assistance to contract consulting services for the compiling, analysis and dissemination of statistical data, including price information, and for the monitoring and review of efficiency and competition indicators. The execution of these two activities will be funded by the technical cooperation operation.
- 2.48 The marketing bill is pending before Congress and is expected to be approved by the third quarter of the year. Once it is approved, and in parallel with the development of the elements of the reform described in the preceding section, the implementing regulations will be prepared with support from the technical cooperation operation, together with the technical rules and specifications required for completing the reform of the legal framework for hydrocarbons marketing.

III. FINANCING AND EXECUTION

A. Borrower and executing agency

- 3.1 The Government of Guatemala will be the borrower of the proposed loan. The executing agency will be the Ministry of Economy (ME), through the program coordination unit (PCU).
- 3.2 The ME was created on May 3, 1945, by Government Decree 28-45. Its main functions include the legal framework for foreign and national investment in the country; policies on consumer protection, promotion of competition and control of unfair competition; regulation of bilateral and multilateral international trade agreements and treaties, and responsibility for their subsequent implementation; promotion of foreign investment and industrial and commercial development, and proposal of policies for their execution; and formulation and execution of the country's tariff policy.
- 3.3 The PCU will be set up within the ME exclusively for the purposes of the program and will act as such, both for the quick-disbursing sector loan and for the technical cooperation loan and the MIF grant.
- 3.4 Regarding the quick-disbursing loan, the PCU will coordinate the execution of the program activities with the MEM, the MCTOP, GUATEL, INDE, EEGSA, the DGAC and the Special Divestiture Committee (CEDE) of the Office of the Commissioner for Modernization of the Executive Branch. For the coordination and implementation of the reform policies, the PCU will have the following specific functions: (i) monitoring of the execution of the program, including all tasks connected with the conditions for the disbursement of the sector loan funds, the IDB technical cooperation loan, and the MIF grant; and (ii) coordination and preparation of the supporting documentation for the submission of disbursement requests to the Bank.
- 3.5 For the purposes of the execution of the technical cooperation loan and the MIF grant, the responsibilities of the PCU are described in Annexes III and IV, respectively.
- 3.6 The MCTOP will have technical responsibility for execution of the program in the telecommunications and civil aviation sectors, while the MEM will have technical responsibility for the program in the area of electricity and hydrocarbons sector reform, and the ME will have technical responsibility for the investment sector part of the program.

B. Financing of the operation

- 3.7 The proposed operation consists of a quick-disbursing loan to the Republic of Guatemala of US\$100 million from the Single Currency Facility, to be disbursed in a first tranche of US\$30 million and three floating tranches totaling US\$70 million to be disbursed independently once the objectives indicated in the sector policy matrix (Annex I) have been achieved. The loan would have a disbursement period of thirty-six (36) months.
- 3.8 The disbursement period and the proposed structure are consistent with the structure of the program and with the scope and complexity of the activities involved in its execution.
- 3.9 The operation also includes a proposal for approval of a technical cooperation loan of US\$7.65 million and nonreimbursable technical-cooperation funding of US\$1.15 million from the MIF. Details of these are included in Annexes III and IV to this document, respectively.

C. Status of compliance with the conditions for presentation to the Board of Executive Directors and for disbursement of the first tranche of the financing

- 3.10 The General Telecommunications Law and the General Electricity Law have already been promulgated by the Executive Branch. The government already has a civil aviation bill and a hydrocarbons marketing bill. These bills only require an absolute majority for approval by Congress. The respective ministries have given their approval in principle and the bills are expected to be approved by Congress in the first half of 1997.

D. Environmental aspects

- 3.11 At its meeting of August 29, 1996, the CMA classified this as a Category III operation, and the CESI approved the environment and social impact report on March 14, including the terms of reference for the preparation of the environmental audits and assessments.
- 3.12 To take care of the problems connected with the environmental aspects of the reform program the following steps have been taken: (i) the sector policy letter includes precise references to the scope and content of the program's policy elements to address the environmental aspects; and (ii) the technical cooperation plan of operations explicitly includes the funds for financing the preparation of the assessments of environmental liabilities, for preparation of the terms of reference for the environmental impact assessments (EIAs), for regulating the environmental aspects of the sector laws, and for strengthening the monitoring and inspection capacity of the body or bodies responsible for environmental matters.

- 3.13 Moreover, the presentation of the operation for consideration by the Bank's Board of Executive Directors, and therefore the start of disbursements from the loan, is subject to the approval of the sector laws in each of the sectors. In the case of the electricity sector, the General Electricity Law specifies that electricity generation and transmission projects must attach the respective EIA, which must be accompanied by an opinion of the National Committee on the Environment (CONAMA). In the case of hydrocarbons marketing, in addition to the environmental impact studies, the bill requires that all facilities, equipment and activities connected with the marketing chain meet the natural resources protection requirements laid down in the implementing regulations and any other applicable legislation or rule laid down by competent authorities. The bill also establishes the obligation to provide free access for inspection of operations, facilities and equipment connected with the marketing activities. The civil aviation bill also provides for free access for inspection purposes, and the obligation to comply with the specific requirements set by ICAO.
- 3.14 In addition, as part of the evaluation of requests for disbursement of the subsequent ("floating") tranches, the environmental regulations of the sector concerned will be checked for currency. Otherwise, such regulations will have to be included in the participation contracts concluded with the private sector. Moreover, these regulations must be supported by the existence of a competent regulatory or supervisory body, or if there is none, by preparation of independent environmental assessments.
- 3.15 On the basis of duly prepared terms of reference, the executing agency will contract consulting services for preparing the diagnostic study of the preexisting conditions, identifying solutions and assigning responsibilities, and for preparing the terms of reference for the EIAs of the new activities to be transferred to the private sector. The consultants will provide background data, recommendations, mechanisms, etc., for accomplishing, *inter alia*, two main objectives: (i) regulation of the environmental aspects of the sector laws; and (ii) inclusion of the environmental aspects in the private sector participation contracts involving these sectors.
- 3.16 The evaluations will include:
- a. the identification and characterization of the environmental aspects connected with the involvement of the private sector in the hydrocarbons, electricity and aviation sectors, including risk identification, allocation of the respective costs, the investment obligations, and the cost-recovery instruments and mechanisms;
 - b. the environmental activities to be considered in the bidding documents and contracts for privatization of the utilities concerned, clearly stating in each concession document and then

in the respective contract who will assume responsibility for the environmental liability;

- c. preparation in coordination with the executing agency of a mechanism for the proper supervision, monitoring and evaluation of the environmental aspects of the contracts, and also for application of the measures to mitigate the environmental impacts connected with the provision of the services.

E. Development impact indicators

- 3.17 In the infrastructure sectors, the mechanism for involvement of the private sector is by means of negotiated contracts. Identification of the development impact indicators will therefore be a part of determining and developing the activities to be privatized. The consulting services for designing and preparing these contracts will include preparation of the database, nonexistent at the moment in the case of civil aviation and incomplete in the case of electricity, and assistance in the formulation of these indicators. Annex V (see also paragraph 3.28) includes a tentative list of what the indicators used for making this evaluation could be.

F. Technical cooperation in support of the program

- 3.18 The project is divided into three subprograms: (i) investment environment; (ii) hydrocarbons; and (iii) civil aviation. The execution of the reform program would be financed with local counterpart funds, funds from this technical cooperation loan, and a grant from the MIF, as detailed in the budget presented in Table 1 of chapter IV, in Annex III.

G. Procurement

1. Import procedures

- 3.19 The proceeds from the loan will be used to reimburse the total foreign exchange cost of eligible imports. The disbursement of the funds pertaining to each tranche will be effected against presentation of the import documentation to be provided by the MFP, which will obtain it from the Directorate General of Customs (DGA). These import documents will be held in the DGA, where they will be available to authorized Bank personnel and the program auditors.
- 3.20 Goods procurement effected with funds from the loan will be carried out in accordance with the Bank's standard procedures. When amounts exceeding US\$5 million are involved, international competitive bidding will be required.
- 3.21 When the costs involved are less than US\$5 million, procurement by the public sector will be carried out in accordance with the established national procedures, provided these are consistent with the Bank's procurement policies. Smaller purchases by the private

sector will be made in accordance with applicable commercial practices and will, when possible, be based on quotations provided by suppliers in at least two Bank member countries.

- 3.22 The disbursements from the proposed loan will conform to the policies established by the Bank regarding sector loans, which provide for retroactive financing of authorized expenditures made up to six months prior to the effective date of the loan contract. The total amount of such retroactive financing is limited to 50% of the total amount of the loan. For application of this condition, the date of the expenditure will be the value date of the remittance of funds to the foreign supplier.

H. Audit and control

- 3.23 The loan proceeds will be disbursed against statements of expenditures to be submitted to the Government of Guatemala. These statements must detail all transactions conducted during the execution period and provide evidence that the eligibility conditions have been met. The information contained in the statements must include data as to type of importation, country of origin, dates and value.
- 3.24 The PCU is responsible for keeping the accounting records and for preparing and submitting disbursement requests. The statements of account of each tranche will be audited by a firm of independent auditors acceptable to the Bank. These statements are to be submitted within 90 days of the last disbursement from each tranche. The audited reports must demonstrate, in accordance with procedures acceptable to the Bank, that the goods in respect of which disbursement requests have been submitted under the respective tranche are eligible for reimbursement from loan proceeds.
- 3.25 The Bank reserves the right to perform ex post examinations of the various documents and stages of each procurement transaction pertaining to the program.

I. Inspection and supervision

- 3.26 The Bank is to establish the inspection procedures necessary for ensuring satisfactory execution of the program. To this end, the borrower will provide all necessary cooperation. The equivalent of US\$1 million from the financing will accordingly be paid into the Bank to cover inspection and supervision.
- 3.27 The borrower and the Bank will hold meetings, at the request of either party, to assess the progress of the program and attainment of the program goals so that the disbursements under each tranche may be made. The executing agency will provide all cooperation necessary to facilitate the holding of such meetings.

J. Program monitoring

- 3.28 In order to provide technical support and assess the progress of the program, the project team will have technical responsibility for the operation and, in coordination with the Country Office, will make periodic visits to Guatemala.
- 3.29 In addition to the missions to assess the loan disbursement requests, the Bank plans to send missions to determine the initial levels and the desired targets for the development impact indicators. Since the condition for disbursement of the floating tranches is directly linked to the privatizations, the development impact indicators for each of the sectors will form part of the evidence that the borrower is required to submit with the disbursement requests for the floating tranches.
- 3.30 In view of the nature of the program, the government has no interest in performing an ex post evaluation of this operation. Instead, the regulatory bodies will monitor the accomplishment of the goals laid down in the concession contracts.

IV. BENEFITS, VIABILITY AND RISKS

A. Benefits

- 4.1 It is hoped that implementation of the program in the infrastructure sectors will make it possible to mobilize private sector resources to fund the expansion, thereby reducing the burden of the financing and operation of these sectors on the national budget. The involvement of private operators should permit increased levels of coverage, improved service quality and reduced service delivery costs, while recovery of production costs will ensure the sustainable development of these sectors.
- 4.2 Implementation of the program should mean that within 24 to 36 months: (i) a private operator will have responsibilities related to the operation and financing of the expansion of La Aurora Airport in Guatemala City, San José Airport (Escuintla) and Santa Elena Airport in Petén; (ii) in telecommunications there will be private operators competing in the provision of long-distance services, local telephone service, wireless and cellular, and a strategic investor will be involved in the operation and financing of the investment in GUATEL; (iii) the transformation of INDE and EEGSA will have been completed, including the vertical unbundling of generation, transmission and distribution functions, and distribution will have been unbundled horizontally in at least two enterprises for Guatemala City and three or four for the rest of the country; (iv) a controlling interest in the capital stock for EEGSA's distribution activities will have been transferred; and (v) there will have been a significant increase in the rate of national and foreign private investment.

B. Viability and risks

- 4.3 The main risk the government will face in proceeding with execution of the program will be political in nature, and will be reflected primarily in the legal sphere through challenges and questions concerning the constitutionality of the laws and instruments that the government and Congress have approved for implementing the reforms. As noted in section B of chapter I, the relevant legal reports prepared for the Bank support the conclusion that these instruments are fully consistent with Guatemala's Constitution and legislation.
- 4.4 The viability of the reform of the electricity sector is based principally on two components, one being the startup of the wholesale market, and the other the privatization of EEGSA's distribution business. Both of these components are faced with major difficulties in the long-term take-or-pay contracts with the private sector. In the case of the wholesale market, these will represent factors that introduce constraints, and over the next

10 to 15 years the scope and the benefits of the reform will be reduced. In the case of the privatization of EEGSA, the generation costs agreed in these contracts will have a fundamental impact on EEGSA's financial stability and could compromise its privatization prospects. Another risk is the lack of autonomy and independence of the CNEE with respect to the MEM as the sector's policy-making authority.

- 4.5 In the case of telecommunications, there is a risk connected with the interest of private strategic investors in participating in GUATEL. The legislation approved is the best suited to the technological advances and developments in the telecommunications market, but it excludes incentives which, at the expense of sector efficiency, have been offered in the recent past in regulatory frameworks as a means for attracting international operators. Telecommunications companies in the United States are currently reassessing their strategic plans in light of the new telecommunications law approved in the United States.
- 4.6 In the case of hydrocarbons, accomplishment of the development objectives in the sector will depend chiefly on how successful the government is in its efforts to mobilize foreign private investment, which is crucial for infrastructure development in the sector. If this investment is not brought in, at best the changes in the legal and regulatory framework would have a marginal effect in a sector that would remain constrained by an oligopolistic market.
- 4.7 Lastly, from the macroeconomic standpoint, the main risks lie in the management of external resources during the transition, since these resources will have to be administered as a purely temporary inflow; there is also the risk connected with the need to increase the tax burden to levels compatible with public spending and exchange stability requirements.

GUATEMALA
SECTOR POLICY MATRIX
INFRASTRUCTURE AND INVESTMENT SECTOR REFORM PROGRAM

ector	Board	First tranche (US\$30M)	Floating tranches (US\$70M)
conomic ment	Maintains a macroeconomic environment consistent with the objectives of the reform program and of the operation.		
environment	The necessary legal instruments have been adopted for proceeding with the program to involve the private sector in the operation, financing and expansion of the activities involving the provision of household public services and basic infrastructure services.		
mmunications	The General Telecommunications Law has entered into effect.		The sector is open to competition a private strategic investor has primary responsibility for GUATEL's operation. (US\$20M)
ity	The General Electricity Law has entered into effect. The new EEGSA distribution tariffs have been put into effect and the general regulations governing application of the General Electricity Law have been issued.		The unbundling (vertical and horizontal) of INDE's generation, transmission and distribution business has been completed. A private strategic investor has primary responsibility for the operations and capital financing of EEGSA's expansion. The administrator of the wholesale market is in operation.
aviation	The civil aviation bill has been submitted to Congress.	The Civil Aviation Law has entered into effect.	A concession for the operation of La Aurora Airport and, based on recommendations arising from the technical evaluation provided for under the program, the concession(s) for the operation of Guatemala's other airports have been awarded. (US\$25M)
carbons	The hydrocarbons marketing bill has been submitted to Congress.	The Hydrocarbons Marketing Law has entered into effect.	

May 20, 1997

SECTOR POLICY LETTER

Mr. Enrique V. Iglesias
President
Inter-American Development Bank
Washington, D.C.

Dear Mr. Iglesias:

Introduction

Since 1992, Guatemala has been carrying out a number of economic adjustment and financial sector reform programs with support from the World Bank and the Inter-American Development Bank, respectively. Currently, the country is immersed in an important process of political, economic and social change to promote sustainable economic growth, comprehensive development and the improved well-being of our entire population. In the political sphere, efforts have been aimed at getting the **Agreement for a Firm and Lasting Peace** signed. This commitment is based on measures designed to guarantee respect for human rights and to promote and strengthen the State based on the rule of law and legal security for the entire population, and concludes an internal armed confrontation of over 36 years' duration. The Agreement for a Firm and Lasting Peace was signed on December 29 last, and the international community responded with significant expressions of support during the Consultative Group meeting held in Brussels at the end of January. These conditions are also serving as a basis for making it possible to move ahead more quickly with the process of structural reforms and consolidation of macroeconomic stability.

Macroeconomic Environment

Within the macroeconomic policy framework, special importance has been assigned to ensuring the consistency and comprehensiveness of economic policy, which requires special coordination of the fiscal, monetary and trade policies.

In this context, the fiscal policy efforts are being aimed at achieving equilibrium in public finances by means of actions that will help increase tax collection, on the one hand, while also fostering efficient use of resources in the priority areas of government responsibility, on the other. During 1996 fiscal policy was strengthened by the adoption of measures targeting both of these goals.

In the area of tax collection, as of January 1, 1996, the value added tax was increased by three percentage points. That same year, the Special and Temporary Solidarity Tax (ISET) was established and a specific

gasoline tax was introduced, to provide resources for the special fund for maintenance of the country's road system. Moreover, in the context of the tax administration, it should be noted that current legislation was improved, including amendments to the Tax Code and the Criminal Code, which now make it possible to close down the businesses of and imprison tax evaders. In addition, the import clearance document assessment system was changed, effective March 1 of this year, to reduce customs discretionary authority.

In April 1997, we submitted a bill to Congress for the creation of a Superintendency of Tax Administration, an authority that would absorb the functions of the present General Directorates of Internal Revenue and Customs. A proposal has also been submitted to Congress for income tax reforms to go into effect on July 1, 1997, in order to expand the tax base and strengthen the tax collection capacity. In addition, a comprehensive process of administrative purging and elimination of tax fraud, tax evasion, and contraband has been undertaken.

Regarding efficient use of fiscal resources, priorities in spending and public investment have been shifting towards education, health, housing, social and productive infrastructure, civil security, and justice.

In 1996, in a harmonious atmosphere of consensus-building, labor mobility was promoted through a reduction in the number of vacancies and other budget cutbacks in areas of minimum social returns, identified by the State modernization project, the approval and implementation of which are vital to achieving greater efficiency. This program initially calls for the reorganization of three ministries: the Ministry of Public Finance, the Ministry of Education and the Ministry of Communications, Transportation, and Public Works. It also provides for submission to the legislature of reforms in the civil service system and in the organizational structure of the Executive Branch.

Monetary policy is aimed at bringing inflation down to a level comparable to international levels, while at the same time strengthening the country's international position, in order to lay the foundations for the stability required for sustainable economic growth. To this end and in order to ensure the effectiveness of monetary policy, a proposed amendment to the Central Bank Charter has been submitted to Congress, which seeks to expand application of the reserve requirement to all liabilities that constitute deposit-taking.

In order to cause a drop in the interest rate without endangering stability, fiscal policy has increasingly been supporting monetary policy.

Trade policy seeks to achieve a successful positioning of Guatemala in international markets together with more competitive participation of the productive sector in the domestic market. Public sector officials and representatives of the private sector, from the highest echelons, have

participated in the formulation of this policy, to ensure that consistent and coordinated actions are adopted that will help to generate an appropriate environment for productive investment and better utilization of infrastructure and services, while also fostering entrepreneurial and marketing work. Moreover, significant progress has been made in trade negotiations with Mexico, which are being conducted jointly with El Salvador and Honduras.

There is also a high-priority agenda of international trade negotiations which, in the spirit of the Miami Summit and in anticipation of the creation of the FTAA by the year 2005, includes the possibility of concluding free trade agreements with the United States, Panama, the Dominican Republic, CARICOM, and the Andean Common Market.

In **tariff policy**, effective January 1, 1996, we reduced the tariff applicable to capital goods imports from 5% to 1%. In addition, as of January 1, 1997, we began to enforce the tariff reduction schedule for Guatemala applicable to raw materials, intermediate goods and finished goods, the aim being to reach a range of 0% to 15% by January 1999. It should also be noted that in 1996 we replaced nontariff restrictions with tariff measures by putting in place tariff quotas that allow the importation of various agricultural products based on the World Trade Organization agreements concluded during the Uruguay Round.

Regarding **exchange policy**, our commitment is to maintain the present exchange system, which allows the exchange rate to be determined by the market and limits the Central Bank's involvement solely to obtaining the foreign exchange needed to meet its external commitments and those of the government plus whatever is necessary to prevent sudden, cyclical or seasonal fluctuations in the rate. A policy of free convertibility and transfer of capital is in force.

With regard to **structural reform**, which is a major component of the sector program described below, we have made significant progress in recent years, chiefly in the areas of price and trade liberalization and financial modernization. However, to take advantage efficiently of the benefits of stability achieved so far in order to foster conditions for sustainable economic growth, it will be necessary to carry the structural reforms further.

The Government of Guatemala is negotiating with **International Monetary Fund** authorities to arrive at an agreement on an economic program for 1997-98 that will facilitate implementation of the peace program in a macroeconomic framework consistent with price stability and a viable external position, in order to achieve sustainable economic growth and a reduction of poverty. The government's economic program serves as a platform to ensure fulfillment of the peace agreements and timely political support, technical assistance and financial cooperation from the international community. In particular, these efforts have the coordinated support of the IDB, the World Bank and the United Nations.

The main component of the program is **strengthening of the financial position of the public sector**, in particular the level of savings, with the aim of achieving a higher level of public investment and social spending.

The program also provides for replacing nonproductive spending with social spending and seeking greater efficiency in services such as education and health. To obtain the resources needed to finance increases in social spending in a climate of sound fiscal balance and to strengthen the public sector's financial position, it will be essential to **increase the tax burden**. This will make it possible to maintain an appropriate level of investment in the medium term once external financial aid reverts to normal levels, thereby preserving macroeconomic stability. The program accordingly provides for gradually increasing the tax burden along the lines established in the peace agreements. It will also include appropriate adjustments to prices and tariffs for public goods and services, in order to ensure that the coverage and present and future quality can be sustained.

Sector reform program

In January 1996, the government of President Arzú acquired along with the Guatemalan people, *inter alia*, the fundamental commitment to promote productive investment to achieve fast-paced economic growth, with a view to comprehensive, sustained and sustainable development while preserving and improving the environment, in accordance with the principles of the social market economy.

The **economic commitment to productive investment** is built into the Government Plan for 1996-2000 as is the need to provide the conditions that will enable the peace agreements to be fulfilled on a timely basis. Our commitment focuses on: (i) the maintenance and establishment of clear, positive and stable rules; (ii) development of competitive and transparent markets, without unfair competition, discouraging the formation of monopolies or oligopolies of any sort, whether private or State-operated; and (iii) elimination of comprehensive subsidies, which will be replaced by exceptional, targeted, temporary and decreasing subsidies.

The amount and components of the quick-disbursing loan and the technical cooperation funding under the infrastructure and investment sector reform program are justified in light of the policies and action guidelines proposed in the Government Plan. We believe that execution of the reforms included in the program will enable us to achieve economic prosperity without discrimination, while safeguarding the right to property, and private and collective enterprise, efficient allocation of economic resources and protection of consumers' rights and of the environment.

1. Infrastructure and hydrocarbons

The regulatory framework will be adjusted, the role of the State institutions redefined and private sector participation promoted, for reasons of efficiency and effectiveness, in the planning, design, construction, financing, operation and maintenance stages of national and local, productive and social infrastructure. The functions of State-owned enterprises will be limited to general regulatory and abstract functions and to supervision and policy formulation. The general goal is to improve and increase the infrastructure and overcome the country's serious deficiencies by expanding it and upgrading its quality.

The reform of the **civil aviation sector** is based on adoption of a new legal framework that redefines the role of the General Directorate of Civil Aeronautics, limiting its functions to supervision and policy formulation. With IDB technical assistance, a civil aviation bill has been drafted that will be sent to Congress in June 1997. This bill regulates the performance of civil aeronautics activities, promotes private participation within a competitive framework of concessions (usufruct and authorizations) and service provision, and supports rational, efficient and safe use of the country's air space.

In the **telecommunications sector**, the reform is based on demonopolization of the market, the adjustment of rates to the real costs of managing and administering the services to ensure a return on the investments, and establishment of a regulatory framework for the privatization of GUATEL. Decree 94-96, General Telecommunications Law, published on November 18, 1996, provides for deregulation of the market, development and use of the radio spectrum under competitive conditions, by means of the public auctioning of usufruct permits, fostering of investment in the sector, and protection of the rights of consumers and of the enterprises providing the service. Regarding the adjustment of the rates and the sale of GUATEL, we are preparing the most viable plan consistent with the country's political and legal conditions.

Our proposed reform of the **electricity sector** is conducive to increasing the supply of electrical energy in the most economical manner to all regions of the country, upgrading the quality of service, adjusting tariffs to real costs, and expanding coverage in energy use while preserving the ecological equilibrium and promoting comprehensive and orderly development of the market. Consequently, on November 15, 1996, Decree-Law 93-96, General Electricity Law, was published, which eliminates generation and distribution monopolies for electrical energy. It also establishes the market regulatory commission, the methodology for calculating tariffs, and open calls for offers in pursuit of service concessions. Regarding the transformation (vertical unbundling) of the National Electrification Institute (INDE) and divestiture (privatization) of the distribution system of the Empresa Eléctrica de Guatemala S.A. (EEGSA), the most viable action plan consistent with the country's political and legal conditions is being worked on. Lastly, for the

calculation of the new electricity tariffs and their implementation we are proceeding as specified in Decree 93-96.

In the **hydrocarbons sector**, the reform will make it possible for hydrocarbons to be supplied in the most efficient way and at the lowest possible cost. The reform accordingly focuses on strengthening market mechanisms in marketing and on determining the prices of petroleum by-products, transparency of the markets and protection of the rights of users and economic agents, and preventing monopolistic practices and unfair competition. To this end, with the IDB's assistance, a hydrocarbons marketing bill has been drafted that was submitted to Congress in May 1997. We have also prepared a plan for the institutional strengthening of the General Directorate of Hydrocarbons in its role as a control, inspection and promotion agency.

2. Investment environment

Our purpose is to create an environment of certainty and confidence that will serve to foster domestic savings and national and foreign private investment. By means of the proposed reforms we are seeking to improve the legal and regulatory framework in order to eliminate barriers to entry into the national markets, ensure uniform treatment for national and foreign private investment and guarantee property rights, including intellectual property. The reform of the sector also includes institutional strengthening of the Ministry of Economy in the promotion of investments and exports and in the calculation of the Consumer Price Index. In addition, our objectives further include design and implementation of new legislation to protect consumers' rights, promote free competition and prevent unfair competition.

Guatemala has acceded to the Multilateral Investment Guarantee Agency (MIGA) and we are currently making progress in negotiations on agreements for the protection of investments at the bilateral level. With the IDB's assistance, the foreign investment bill and the bill for the promotion of the market and competition have been drafted and will be sent to Congress in the second quarter of 1997. Regarding the laws on intellectual property, we have prepared bills to strengthen current legislation on copyright, trademarks and patents. We are currently reviewing the content of these bills for their timely submission to Congress.

3. Environmental aspects

The environmental situation in Guatemala is characterized by rapid deterioration over the past 30 years as a result primarily of poverty due to lack of opportunities, the negligible or nonexistent effectiveness of incipient environmental policies, the absence of environmental criteria in the formulation of economic and social policies and the lack of consideration regarding environmental conservation criteria in productive investments.

The government's strategy for reversing this situation is based on policies and guidelines for actions that promote the proper and efficient use of environmental impact assessments, the establishment of monitoring processes applying appropriate environmental standards, the establishment of regulations, rules and standards in each sector and the inclusion in environmental management of economic incentives based on environmental efficiency, efficacy and equity in the social and economic costs and benefits.

The reforms of the infrastructure and hydrocarbons sectors meet various of the environmental aims of our Government Plan, particularly with the recovery of costs connected to resource conservation and sustainability of the environment; the inclusion of environmental guidelines in the new legal and regulatory frameworks for the provision of public services; and the preparation of diagnostic studies and environmental assessments and audits so as to include in private contracts the most appropriate mechanisms and structures of incentives for future service delivery arrangements.

Concluding Considerations

The infrastructure and investment reform program contains high-priority actions provided for in the Government Plan to combat poverty and achieve sustainable development. The Agreement for Firm and Lasting Peace demands timely responses and has become one more incentive for moving ahead as quickly as possible with the policies and approaches described in the Government Plan, while remaining fully consistent with the objectives of the proposed reform program.

In conclusion, the specific outcomes achieved and the efforts that the Government of Guatemala has made to date to promote equality of opportunity, change the functions of the State enterprises, promote competition and attract national and foreign private investment, constitute our best evidence of compliance with the economic commitment to productive investment.

Juan Mauricio Wurmser
Minister of the Economy

José Alejandro Arévalo Alburez
Minister of Public Finance

PLAN OF OPERATIONS

**TECHNICAL COOPERATION LOAN IN SUPPORT OF THE
PROGRAM OF REFORM IN INFRASTRUCTURE AND INVESTMENT
(PRII)**

EXECUTIVE SUMMARY

BORROWER AND GUARANTOR:	Republic of Guatemala
EXECUTING AGENCY:	Ministry of Economy, through a program coordination unit (PCU)
AMOUNT AND SOURCE:	IDB: US\$ 7.65 million (OC) Local counterpart funding: US\$ 2.35 million Total US\$10.00 million
FINANCIAL TERMS AND CONDITIONS:	Execution period: 32 months Disbursement period: 36 months Interest rate: variable Amortization period: 20 years Grace period: 42 months Inspection and supervision: 1% Credit fee: 0.75% Currency: U.S. dollars (Single Currency Facility)
OBJECTIVES:	The purpose of this technical cooperation is to fund the Program of Reform in Infrastructure and Investment which the Bank is supporting in parallel with a quick-disbursing loan (GU-0019). The funds from this Bank technical cooperation loan will be used to finance activities connected with reforms of the investment framework and of the oil and gas and civil aviation sectors. The financing is complemented by a MIF grant (TC-96-09-17-6) for inclusion of the private sector in the provision and expansion of services in the civil aviation sector.
DESCRIPTION:	The technical cooperation is structured in three subprograms, one for each of the sectors. In the investment framework reform subprogram, the funds will be used to finance preparation of the following components: (a) promotion of foreign investment; (b) strengthening of the Program of Commercial Attachés in Investment and Tourism (PACIT);

(c) consumer protection, promotion of competition and protection of intellectual property rights; and (d) the National Income and Expenditure Survey. The oil and gas sector subprogram includes the following components: (a) institutional strengthening of the General Directorate of Hydrocarbons (DGH); (b) development of price logistics; (c) preparation of environmental regulations; and (d) regulatory framework for marketing. The civil aviation subprogram has the following components: (a) institutional strengthening of the Civil Aviation Directorate (DAC); (b) Strategic Plan for Air Traffic Control; and (c) environmental conservation.

**ENVIRONMENTAL
CLASSIFICATION:**

The Environment Committee, at its meeting of August 29, 1996, classified this as a Category III operation. The Environment and Social Impact Committee approved the environmental summary on March 14, 1997.

BENEFICIARIES:

The direct beneficiaries of the technical cooperation will be the Economic Affairs Investigation Bureau (*Fiscalía Económica*) and the following institutions and programs attached to the Ministry of Economy: National Statistics Institute, PROGUAT and PACIT; the General Directorate of Civil Aviation in the Ministry of Communications, Transportation and Public Works; and the DGH in the Ministry of Energy and Mines. To tackle these complex reforms, this financing will enable the government to engage experts for specialized consultancies involving financial, legal, technical, environmental and economic analyses and evaluations connected with the components of the programs.

RISKS:

The main risk has to do with the scale and complexity of the program, which will require a program coordination unit (PCU) that will also be the program's chief coexecuting unit. A second risk is connected with the highly specialized profile of various of the main consultancy services to be contracted. To counter this risk, the disbursement conditionality is based on the Bank's procurement procedures in general, and on the Bank's participation in the identification and selection of consultants and in drawing up their terms of reference and reviews of their work. Lastly, there is a risk associated with the administration of the resources, and in particular with the procedures and timeframes for contracting consultants. To offset

this risk, the proposed operation recommends contracting UNDP assistance.

**EXCEPTIONS TO BANK
POLICY:**

It is proposed that direct contracting be authorized of UNDP as the agency to perform administrative support activities for the PCU for the contracting of the consultancy services required. For the DGAC institution-strengthening component, it is proposed that the International Civil Aviation Organization (ICAO) be contracted directly.

For the selection of consultants it is proposed that a least-cost selection method be used, whereby a "minimum acceptable technical level" is established for rating the quality of technical proposals. Bids are submitted in two separate envelopes. The technical proposals are opened first and evaluated. Those that do not meet the acceptable minimum level are discarded and only the financial proposals submitted by the remaining bidders are opened. The firm offering the lowest price is then selected. With this method, it is understood that the definition of acceptable minimum takes into account that proposals above that acceptable minimum will only be competing in terms of cost. The minimum level will be explicitly stated in invitations for proposals (see paragraph 3.7).

**SPECIAL
CONTRACTUAL
CONDITIONS:**

The following conditions precedent to disbursement of the loan are proposed: (i) the government has concluded a support agreement with UNDP for administration of the project; (ii) the PCU has been set up; and (iii) the work plan for execution of the program has been submitted (see paragraph 5.3).

In addition, the technical cooperation (TC) and grant agreements will include standard Bank and MIF conditions relating to, inter alia, audits, reports, inspections, evaluation of the TC and contracting of consultants.

The resources of this TC relating to each of the subprograms will only be eligible for disbursement once the respective legal frameworks have been approved (see chapter II).

International competitive bidding will be required for procurement of goods valued at over US\$300,000. Contracting for works is not provided for under the program.

I. OBJECTIVES

- 1.1 The purpose of the reforms is to develop and strengthen unrestricted competition, eliminate market monopolies and adopt clear and transparent legal frameworks, together with regulatory frameworks, and institutional structures that afford reasonable economic and legal certainty.
- 1.2 The reform of the investment framework is designed to establish a sound framework for protecting consumers, promoting competition in the market, mobilizing local and external private investment and estimating household consumption in order to update the Consumer Price Index (CPI). The oil and gas sector reform is intended to promote efficient marketing of those products. The reform of civil aviation is aimed at involving the private sector in the operation and expansion of capacity of this service.

II. DESCRIPTION OF THE PROJECT

- 2.1 The project is structured in three subprograms: (i) investment framework; (ii) oil and gas; and (iii) civil aviation. The execution of the reform program would be financed with local counterpart funds, resources from this technical cooperation loan, and a MIF grant, in accordance with the itemized budget set out in Table 1 in chapter IV.

1. Subprogram I. Reforms of the investment framework 1/

- 2.2 This subprogram comprises the following components:
 - (a) Promotion of foreign investment, including the creation, organization and training of staff of PROGUAT, the agency that would be responsible for promoting foreign investment and exports; staff training, both for the one-stop investment window and for PROGUAT; equipment procurement and installation of information systems; and organization and preparation of forums and promotion materials.
 - (b) The strengthening of PACIT, which includes an evaluation of the program; its expansion, through pilot programs for opening new commercial attaché offices; the training of commercial attachés; and equipment procurement.

1/ Details of the main problems in the present investment environment and of the nature and scope of the program are given in Appendix 1 to this annex.

(c) Consumer protection, promotion of competition and intellectual property, which includes the creation, organization and training of staff of the agency responsible for oversight and control of the laws governing competition, consumer protection and intellectual property; equipment procurement; preparation of events and materials to publicize the new legislation and the operation and procedures of the Economic Affairs Investigation Bureau.

(d) Execution of the National Household Income and Expenditure Survey for updating of the CPI, which comprises: updating of maps, the pilot survey, printing of documents, training for and execution of the survey, data coding and processing.

- 2.3 According to the proposed schedule, it is expected that the Foreign Investment Law will be passed by Congress in mid-1997, and the Law on Promotion of Competition and Consumer Protection in the third quarter of 1997. The promotion activities for investment and exports will be carried out in the next 12 months. A period of 24 months is expected to be required for conducting the National Household Income and Expenditure Survey and tabulating the findings. The aforesaid proposed periods are calculated from the date of signature of the technical cooperation agreement.

2. Subprogram II: Reform of the oil and gas sector

- 2.4 This subprogram includes the following components:

(a) Institutional strengthening, comprising: evaluation of the organization and management of the DGH; devising a strategy for the international promotion of investment in exploration and production; equipment modernization; establishment of an oil and gas exploration databank; and training programs.

(b) The logistics of supply and pricing, which will include the gathering, compiling, analysis and publication of prices, together with monitoring and review of efficiency and competition indicators.

(c) Environmental protection, which will include: (i) preparation of terms of reference for environmental impact assessments (EIAs) and environmental damage assessments; (ii) development and preparation of environmental standards; and (iii) training of the agency responsible for compliance monitoring for environmental standards.

(d) The regulatory framework of the new Hydrocarbons Marketing Law, comprising preparation of the regulations once the law is approved.

3. Subprogram III: Civil aviation reform

- 2.5 This subprogram includes the following components:

(a) Strengthening and training of the DAC as regulatory and oversight agency for sector activities, which includes: (i) the design and development of the new organization, including the writing of operating and procedures manuals, and a management information system; (ii) review and adaptation of technical standards and procedures to bring them up to international standards, which will call for new operating manuals for application of technical standards on flight safety and protection; (iii) computer systems and equipment; and (iv) training and retraining of management and technical personnel.

(b) Involvement of the private sector in air transportation infrastructure, which will be financed with a MIF grant (see Annex IV), with support from the Executing Unit (CEDE), with funding from the technical cooperation loan proposed herein.

(c) Environmental protection: (i) drafting of terms of reference for EIAs, and environmental assessments; (ii) development and preparation of environmental standards; and (iii) training of the agency that will monitor compliance with environmental standards.

III. ORGANIZATION AND EXECUTION

3.1 The borrower will be the Republic of Guatemala, and the executing agency will be the Ministry of Economy, through a program coordination unit (PCU) set up specifically for this purpose, which will be supported by units with technical responsibility for execution of each of the respective subprograms. For the administration of this operation, the PCU will be assisted by UNDP (hiring of consultants and equipment procurement).

3.2 For the civil aviation sector reform subprogram, technical responsibility will lie with the DGA of the Ministry of Communications, Transportation and Public Works, and with the Special Committee on Divestiture (CEDE) of the Office of the Commissioner for Modernization of the Executive Branch. For the oil and gas sector subprogram, the agency with technical responsibility will be the General Directorate of Hydrocarbons (DGH) of the Ministry of Mines and Energy. For the investment framework subprogram, the Ministry of Economy will have technical responsibility.

1. Functions of the executing unit (PCU)

3.3 The PCU will be coexecuting agency for the technical cooperation. It will focus on coordination, liaison and review of the activities of the other agencies participating in the program. The PCU's main duties will be to (i) administer the technical cooperation resources pursuant to the contract; (ii) submit reports required

under the agreement and perform the pertinent monitoring and evaluation activities; (iii) coordinate the work of the other participating agencies; (iv) supervise and monitor UNDP's participation in the technical cooperation; (v) coordinate with the Bank for the planned activities; (vi) ensure the consistency of the TC-supported activities with the policy elements for the reform program; (vii) coordinate with the other participating agencies for compliance with the contractual conditions, preparing the pertinent documentation; (viii) submit disbursement requests to the Bank; (ix) submit audited financial statements to the Bank as required in the agreement; (x) oversee the performance and evaluation of the consultancy services engaged, with assistance from the respective technical unit; and (xi) respond to reasonable requests from the Bank for information concerning the execution of the technical cooperation.

- 3.4 To perform its coordination, liaison and coexecuting functions, the PCU will be set up with a skeleton staff of one coordinator, one administrator and three assistants, plus a technical advisor in each technical executing unit.
- 3.5 The core function of the units having technical responsibility for the different TC subprograms will be to coordinate the various consultants' work and serve as technical counterpart for the outside consultancy services. Their other functions will be to (i) prepare the documentation needed to engage the required services, in coordination with the PCU and in concert with UNDP; (ii) monitor and prepare progress reports, for submission to the PCU; (iii) assess consultant performance, and (iv) prepare technical documentation requested by the PCU.

2. Implementation arrangements

- 3.6 The government has requested that UNDP furnish administrative support to carry through this technical cooperation. This would expedite the contracting of consultants and the procurement of goods. This mechanism, employed by the Bank in other operations now under way, has proven to be effective, drawing on UNDP's experience in the areas in question, so it is recommended that the government's request that UNDP administer goods and services contracting be accepted. UNDP meets the criteria specified in policy GS-603 for the purposes stated.

3. Procedures for selecting and hiring consultants

- 3.7 For the selection of consultants it is proposed that a "least-cost" selection method be used, whereby a "minimum acceptable technical level" is established for rating the quality of technical proposals. Bids are submitted in two separate envelopes. The technical proposals are opened first and evaluated. Proposals that do not meet the acceptable minimum level are discarded, and only

the financial proposals from the remaining bidders are opened. The firm offering the lowest price is then selected. It is understood in this method that the definition of acceptable minimum takes into account that proposals above that acceptable minimum will only be competing in terms of cost. The minimum level will be expressly stated in invitations for proposals.

- 3.8 The recommendation to use the minimum-cost method for selecting consulting firms is justified by the nature of the work required for the proposed program. That work is generally complex, but appropriate standards and adequate professional practices are already in place. Experience shows that frequently when technical offers are ranked, a certain number of them will be technically acceptable and suitable for the services required. The recommended methodology not only transfers to the consultants the weight of responsibility for drawing up technically sound proposals, but also obliges them to make them economic and competitive.
- 3.9 The administrative and operating side of procurement and consultant contracting to be funded by the technical cooperation will fall to UNDP, under the terms of an ad hoc agreement to be approved by the Bank. This will be made a condition precedent to the first disbursement out of the technical cooperation funds.
- 3.10 Disbursements will be processed in accordance with the Bank's normal procedures. At the PCU's request the Bank will deposit the funds in a UNDP account, with the object of giving it flexibility in managing the funds. The accounting records will be audited by a firm of independent public accountants acceptable to the Bank, for subsequent submittal to the Bank.
- 3.11 Basic responsibility for the operation rests with the Finance and Infrastructure Division of Regional Operations Department 2, through the project team for the Bank (GU-0019) and MIF (TC-96-09-17-6) operations in support of the reform program. The operation will be administered through the Bank's Country Office in Guatemala, in accordance with the relevant current rules.

IV. COST AND FINANCING

- 4.1 The total cost of carrying through the reforms is the equivalent of US\$11.15 million, of which the Bank would contribute US\$7.65 million through a loan from the ordinary capital, to support implementation of the reforms associated with the investment framework, oil and gas sector, and institution-strengthening for civil aviation, and a US\$1.15 million grant from the Multilateral Investment Fund (MIF) would be provided to assist with the component for privatization of the National Airports

System (Annex IV). The project memorandum for the latter operation (MIF/AT-130) was distributed to the Donors Committee for consideration on May 16, 1997. The government would furnish US\$2.35 million in counterpart funding. Table 1 summarizes the budget and Tables 2, 3 and 4 give a breakdown of the cost and financing for each sector.

Table 1
Program execution budget
(in thousands of U.S. dollars)

No.	Subprogram	IDB	MIF	Local	TOTAL
1.	Reform of the investment framework	4,000		1,270	5,270
2.	Oil and gas sector	590		80	670
3.	Civil aviation	1,800	1,150	900	3,850
4.	Program coordination unit	400			400
5.	Contingency	500		100	600
6.	Finance charges (inspection and supervision, interest, credit fee)	360			360
	TOTAL COST	7,650	1,150	2,350	11,150

- 4.2 The technical cooperation will be executed over a period of 32 months and the disbursement period will be 36 months, counting in both cases from the effective date of the agreement.
- 4.3 The Bank's funds will be used mainly for the contracting of individual consultants, consulting firms and procurement of goods and materials for the activities envisaged in the program, following the Bank's usual policies and procedures, with due consideration of the exceptions requested in this document. The government's contribution will defray the cost of administration and supervision, including the fee for UNDP's support services.
- 4.4 The technical cooperation funding will also be used to finance part of the setup and operation of the PCU, during the execution period. The salaries of the professional staff and equipment necessary for PCU operation will be financed in this way.
- 4.5 In accordance with current provisions, the terms and conditions of the financing will be as follows: (i) amortization period: 20 years; (ii) interest rate: variable, corresponding to the ordinary capital; (iii) disbursement period: 36 months; (iv) grace period:

42 months; (v) credit fee: 0.75% on undisbursed balances; and (vi) inspection and supervision charge: 1% of the amount of the financing. The financing will be charged to the Single Currency Facility in U.S. dollars.

Other financing

- 4.6 In addition to the proposed technical cooperation loan, funding will be forthcoming from the government, the Bank of Guatemala, and private enterprise to strengthen the PACIT program, and USAID and private sector funds will contribute to the institutional reform of intellectual property.

V. MONITORING AND REPORTS

A. Monitoring of the project

- 5.1 The project will be evaluated on a continuous basis, by means of the reports and evaluations listed below. The Bank's Country Office in Guatemala will be responsible for administering the execution of the project and will perform the periodic supervision activities. Reports will be prepared by the PCU and will be submitted to the Bank in accordance with the agreed work plan.

B. Project reports

- 5.2 The Ministry of Economy, through the PCU, will prepare and submit to the Bank the reports described below.

a. Initial report (work plan)

- 5.3 As a condition precedent to the first disbursement, the PCU is to submit a work plan, based on the matrix agreed with the Bank. This is to be a very brief report focusing on the following: (i) the schedule for the first six months for activities of each subprogram; and (ii) performance indicators and the means for verifying them for each activity.

b. Progress reports and monitoring meetings

- 5.4 Within 30 days after the end of each six months of execution, counting from the effective date of the agreement, a progress report is to be submitted. This report will evaluate what has been accomplished compared with the work plan and will propose an updated version of the work plan for the next six months. The progress report will include details of budget performance and of outputs and outcomes achieved.

- 5.5 In accordance with the progress made in the substantive elements of the reform program, meetings will be held with the project team for monitoring and evaluation of the program (GU-0019). The purpose of these meetings will be to identify special issues or problems that call for adoption of measures not included in the program and reformulations of the technical cooperation loan.

c. Final report

- 5.6 Based on the progress reports submitted to the Bank, within two months of completion of execution of the technical cooperation subprograms, a final report will be submitted, summing up the activities carried out and the results obtained, and evaluating them in relation to the objectives initially set for the operation.

Table 2
Program of reforms of the investment framework
(in thousands of U.S. dollars)

	Component	IDB (OC)	Local (GU govt.)	TOTAL
A.	Promotion of foreign investment	1,000	180	1,180
	1. Organization and startup of PROGUAT	250	30	280
	2. Training of one-stop window and PROGUAT staff	100	50	150
	3. Equipment and information systems	100	50	150
	4. Forums and promotion materials	550	50	600
B.	Strengthening of PACIT (Program of Commercial Attachés in Investment and Tourism) ^{2/}	1,000	400	1,400
	1. Evaluation and monitoring of the program	170		170
	2. Staff training	260		260
	3. Equipment and materials	570		570
C.	Consumer protection, promotion of competition, and intellectual property	1,000	490	1,490
	1. Organization and startup of the Bureau	200	50	250
	2. Equipment and materials	150	50	200
	3. Staff training	400		400
	4. Consumer/producer education campaigns	250	50	300
	5. Strengthening of the Register of Industrial Property plus CARPIN ^{3/}		340	340
D.	National Income and Expenditure Survey	1,000	200	1,200
	1. Updating of maps	50		50
	2. Sectorization and pilot survey	15		15
	3. Document printing	20		20
	4. Training and conducting of survey	835		835
	5. Critique and coding	80		80
	6. Data processing		115	115
	7. Administrative support		85	85
	Total	4,000	1,270	5,270

^{2/} The local counterpart for this component will come from the Ministry of Foreign Relations (70%), Bank of Guatemala (17%) and the private sector through the Trade Association of Nontraditional Exporters (AGEXPRONT) (13%).

^{3/} Local counterpart funding from USAID (US\$300,000) and private sector (US\$40,000).

Table 3
Program of reform of the oil and gas sector
(in thousands of U.S. dollars)

	Component	IDB (OC)	Local	TOTAL
A.	Institutional strengthening of the General Directorate of Hydrocarbons (DGH)	260	30	290
	Control, compliance monitoring, promotion, one-stop window	80		80
	Exploration and investment promotion	50		50
	Exploration: Databank	40		40
	Equipment	90	30	120
B.	Supply and price logistics	80	10	90
C.	Environmental conservation	150	20	170
	Environmental assessments and terms of reference for EIAs	40		40
	Preparation of environmental standards	60		60
	Training of the environmental agency (compliance monitoring)	50		50
D.	Regulatory framework for marketing	100	20	120
	TOTAL	590	80	670

Table 4
Program of civil aviation reform
(in thousands of U.S. dollars)

	Component	IDB (OC)	MIF	Local	TOTAL
A.	Institution-strengthening	900		300	1,200
	Design/development organization and management information system	300		50	350
	Technical regulations and standards <u>1/</u>	250		100	350
	Computer systems and equipment	100		50	150
	Training and retraining	250		100	350
B.	Private sector participation	450	1,150	550	2,150
	(i) Airports	200	1,150	500	1,850
	Air transp. consultant <u>2/</u>		450	150	600
	Legal consultant		400	100	500
	Financial consultant		300	100	400
	CEDE	200		150	350
	(ii) Air traffic control	250		50	300
C.	Environmental conservation	150		50	200
	Environmental assessments and terms of reference for EIAs	40			40
	Preparation of environmental standards	60		25	85
	Training of environmental agency (compliance monitoring)	50		25	75
D.	Contingency	150			150
E.	Inspection and supervision	150			150
	Total	1,800	1,150	900	3,850

1/ Direct contracting of ICAO.

2/ Direct invitation, to draw up short-lists.

REFORM OF THE INVESTMENT FRAMEWORK

I. Main issues

- 1.1 From this standpoint, the reason for the program is the sluggish growth in private investment because appropriate legal, institutional and statistical frameworks as required by the new conditions prevailing in the global and national economies are lacking.
- 1.2 National legislation: (i) in the case of intellectual property, legislation is either nonexistent or too outdated to be of any use in the new circumstances ensuing from the globalization of the economy and technological progress; (ii) in the case of foreign investment, the legislation is scattered in different bodies of law, which introduces uncertainty and raises transaction costs; (iii) in the case of consumer protection and competition, the legislation does not offer appropriate protection for consumers or producers, nor does it repress anticompetitive practices.
 - a. Intellectual property
- 1.3 The protection of copyright, trademarks and patents does not meet the business community's current requirements or offer assurances such as will attract heavier flows of national and foreign investment. The treatment accorded by Guatemala is not uniform and introduces distortions and obstacles into international trade. In addition, the legislation does not provide the level of assurances and protection required by the WTO in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).
- 1.4 For patents, the existing legislation does not consider: (i) the patentability of pharmaceutical, agrochemical and food products; (ii) the principle of international expiration, according to which the rights conferred by a patent will produce no effect when the patented product has been legitimately placed in national or international trade; (iii) compulsory licensing in the event of abuse of a dominant market position hampering unrestricted competition, on the part of a patent holder; (iv) substantive examination by foreign patent offices or authorized institutions, by means of agreements to expedite the registration process; and (v) provisions concerning industrial secrets protected by certain articles of the Commercial and Criminal Codes.
- 1.5 For copyright, the current legislation, in effect since 1954, is incomplete and deficient, because it does not cover the rights of performers, producers of phonograms and radiobroadcasting

organizations, which means that they can be defrauded of their rights owing to the new copying technologies now available. Neither does it include specific protection for computer programs.

- 1.6 Trademark legislation has not been updated since the early 1970s as regards trademarks proper, signs, names or designations used in advertising, trade names, emblems, geographic indications and appellation of origin, and as regards the repression of unfair competition in these areas; in particular, there are no specific provisions for protection of well-known marks.
- 1.7 Regarding registration procedures, the system does not enable tight control over the novelty of products or procedures for which patents are being sought, since because of the lack of mechanisms and personnel, the patentability of products and procedures arises when they have already passed into the public domain in other countries. Similarly, in the case of trademarks, the process is slow, inefficient and costly.

b. Foreign investment

- 1.8 Despite the fact that the Guatemalan Constitution guarantees equality of treatment for foreign investors, the laws covering their guarantees and rights in matters such as private property, expropriation and repatriation of foreign exchange are scattered throughout the country's legal system or refer to these topics implicitly. Moreover, Guatemala is one of the few countries in Latin America without a foreign investment statute, which places it at a disadvantage vis-à-vis other countries of the region.
- 1.9 Guatemala also does not possess parameters for the negotiation of bilateral investment treaties that establish nondiscriminatory and even-handed treatment for all investors, regardless of their country of origin.
- 1.10 There is no database that could serve for monitoring trends and levels of foreign investment. Because of the Ministry of Economy's lack of resources and capacity, investment and export promotion is not being conducted at the levels the country needs.

c. Consumer protection and promotion of competition

- 1.11 Current consumer affairs legislation, in effect since 1985, emphasizes consumer welfare without reference to market relations between producers and consumers. The legislation on promoting competition, which takes in restraints on anticompetitive practices and unfair competition, is inadequate.
- 1.12 At the present time the Ministry of Economy is not in a position to adequately protect consumers or to inhibit unfair competition, owing to the lack of a suitable legal framework and of resources to

effectively enforce the law. Moreover, consumers are not accustomed to asserting their rights or meeting their obligations on contracts.

II. Objectives of the reform

- 2.1 The object of the reform is: (1) the adoption of new legal frameworks for (i) strengthening legislation to protect copyrights and associated rights, patents and trademarks; (ii) establishment of legal and administrative mechanisms that grant uniform treatment and afford legal certainty for national and foreign private investors; and (iii) repression of anticompetitive practices, and effective consumer protection; and (2) strengthening of the institutional capacity of the Ministry of Economy for investment and export promotion.
- 2.2 The main goals of the strategy are the following: (1) reform of the legal framework, which includes: (i) updating of intellectual property laws (copyrights and associated rights, trademarks and patents) to the TRIPS agreement level; (ii) accession to the Paris Convention (patents); (iii) consolidation in a single instrument of all elements pertaining to foreign investment, such as national treatment, guarantees, rights and obligations of foreign investors; and (iv) establishment of a **comprehensive** law covering consumer protection and competition promotion aspects, including repression of anticompetitive practices; and (2) institutional strengthening of the Ministry of Economy, comprising: (i) restructuring of the National Export Promotion Council (CONAPEX) to include investment promotion, through PROGUAT; (ii) expansion of the network of Guatemalan trade offices abroad, under the PACIT program; and (iii) conducting of the National Household Income and Expenditure Survey to obtain data on which to base the weightings used in calculating the CPI.

III. Policy elements of the program

- 3.1 The draft Foreign Investment Law, prepared with Bank assistance, seeks to establish clear, stable, positive general rules for all investors. This bill is ready for consideration by the Executive Branch and is based on completely equal treatment for national and foreign investors. It includes the following: (i) local or national treatment for foreign investors; (ii) the most-favored-nation clause, a basic element in negotiation of bilateral investment treaties; (iii) protection of property and limitations, principles which are included in the Constitution but the drafters have opted to repeat them in the law; (iv) the principle of freedom

of entry of investment funds into the country and freedom to remit profits, including nondiscriminatory access to available foreign exchange; (v) subrogation of insurance; (vi) settlement of disputes by arbitration; and (vii) recognition of private ownership, and of the special cases of expropriation and compensation, in accordance with constitutional principles.

- 3.2 The draft Law on Consumer Protection and Promotion of Competition, prepared with Bank assistance, establishes a new legal framework based on principles of economic efficiency, in which the welfare of consumers includes producers, and on the *per se* (reasonableness determination) doctrine. The draft covers consumers, users, suppliers, procurement of goods and services, prohibition of practices that impede, restrict or falsify competition, acts of unfair competition, unlawful publicity, procedures, penalties and establishment of the agency responsible for administering and enforcing the law.
- 3.3 The draft Law on Copyright and Associated Rights updates the legislation and encourages creation and dissemination of works, recognizing and protecting the rights of authors, performers, producers of phonograms, broadcasting organizations and computer programs.
- 3.4 The draft Law on Patents, Utility Models, Designs and Industrial Secrets promotes the creation, introduction and use of new technologies, permitting patentability of any product or process, with certain internationally accepted exceptions. The law further extends the period of protection from 15 to 20 years; includes the principle of international expiration, which discourages the use of patents as a means for impeding free trade in goods, for the benefit of consumers; and includes compulsory licensing to prevent abuses of dominant market positions by patent holders. Regarding registration of inventions, it authorizes the Register to approach institutions authorized for the purpose or foreign patent offices, with which agreements for performing substantive examinations are concluded. The bill also strengthens protection for industrial secrets and consolidates in a single chapter the provisions currently scattered throughout Guatemalan legislation. Regarding criminal and civil penalties, infringements are defined and imprisonment for four to six years is prescribed for offenders.
- 3.5 The revamping of the Central American Agreement for Protection of Industrial Property (trademarks, trade names or emblems, geographic indications and appellation of origin, and names, signs and designations used in advertising) seeks to update the legislation, with due regard to present-day trends, in regard to protection of distinctive signs, in order to respond to the needs of regional and international trade in products and services. The reforms especially seek to eliminate speculative registration of trademarks by introducing mechanisms that promote their mandatory use in fair

and honest trade terms. Protection of well-known marks is also included.

- 3.6 Accession to the Paris Convention introduces protection of industrial property in the broadest meaning of the term, which takes in industries proper, trade, agricultural and extractive industries, and man-made or natural products, together with the various kinds of industrial patents, such as import and improvement patents, certificates of addition, etc. Accession to the Convention will also imply according national treatment, with respect to the benefits provided by the respective law, to nationals of all member states of the Convention.

IV. Plan of action and status of program

- 4.1 Improving the investment climate will entail approval of new legal frameworks, which were prepared with Bank assistance, and which have already been agreed on by the different sectors concerned.
- 4.2 Foreign Investment Law: To begin with, and with the assistance of an external consultant hired by the Bank, a seminar was organized to discuss the main thrusts and basic principles for formulation of the law. A committee was formed with government and private sector participation which, with the help of an external consultant, has assumed responsibility for discussing and preparing the final version of the draft law. At the present time, review by the legal counsel to the President of the Republic and to the Ministry of Economy is pending. Approval by Congress is expected in mid-1997.
- 4.3 Law on Consumer Protection and Promotion of Competition: After an initial seminar, a working committee was formed of private sector, government and research institute representatives, with responsibility for discussing and drafting the proposed law. It is currently being assisted by an external consultant hired by the Bank to review the draft bill. This process is expected to be completed by late May 1997, when the legal advisers to the Ministry of Economy issue their opinion. Congressional approval is expected in the third quarter of 1997.
- 4.4 Draft bills on intellectual property rights (copyright, patents and trademarks) have been reviewed and commented upon by a Bank consultant in order to strengthen their scope and content. The amendments that will be made to the existing laws will meet TRIPS requirements.
- 4.5 Law on Copyright and Related Rights: The bill was drafted initially with USAID assistance and agreed on with the private sector, particularly cable (TV) companies and computer companies.

It is currently being reviewed by legal advisers to the Ministry of Economy. Approval by Congress is expected in the third quarter of 1997.

- 4.6 Central American Agreement on Protection of Industrial Property (trademarks): The first time this was submitted to Congress (January 1996), the Commissions on Foreign Relations and Legislative and Constitutional Affairs issued a negative joint opinion. When resubmission was attempted (February 1996), the procedure was ruled incorrect and the agreement was ordered shelved for a year. Before it is submitted to Congress for a third time, the WTO is being consulted regarding the treatment to be accorded to "well-known marks" and conflicts that might arise in the national legislation concerning TRIPS provisions, in order to avert another negative opinion. Approval is expected in the first quarter of 1998.
- 4.7 Accession to the Paris Convention (patents): The proposed law has received favorable opinions from the Ministry of Economy and Foreign Relations. Approval is expected in the third quarter of 1997.
- 4.8 Law on Patents, Models, etc.: The bill was initially drafted with USAID support and agreed on with the private sector. The legal advisers to the Ministry are currently making a final review. Approval is expected in the third quarter of 1997.
- 4.9 The action plan for strengthening the investment and export promotion capacity of the Ministry of Economy includes (i) organizing and starting up PROGUAT to promote investment and exports; (ii) evaluating the PACIT program with a view to its reorganization and expansion; (iii) organizing and starting up the bureau for consumer protection and promotion of competition; and (iv) conducting the National Income and Expenditure Survey. It is expected that these components will be carried out in 1997 and 1998. To finance these activities, it is being proposed that the Bank provide a technical cooperation loan of US\$4 million from the ordinary capital. Also available will be about US\$1.27 million in local counterpart funding from the government, the private sector and USAID.

INFRASTRUCTURE AND INVESTMENT SECTOR REFORM PROGRAM

MULTILATERAL INVESTMENT FUND

CIVIL AVIATION SECTOR REFORM AND PRIVATE SECTOR PARTICIPATION

(TC 96-09-17-6)

I. COUNTRY ELIGIBILITY

- 1.1 The Donors Committee of the Multilateral Investment Fund (MIF) declared Guatemala eligible for all types of MIF financing on March 30, 1995.

II. FRAME OF REFERENCE

- 2.1 The MIF financing forms part of the support for the infrastructure and investment sector reform program (GU-0019). That program's purpose is to reform the investment framework and the civil aviation and hydrocarbons sectors.
- 2.2 The MIF resources will be supplemented with a prospective quick-disbursing sector loan (GU-0019) to meet Guatemala's external financing needs, and with a reimbursable technical cooperation loan to implement reforms in the investment and the civil aviation and hydrocarbons sectors. In parallel, the World Bank is preparing a Technical Assistance Loan (TAL) which includes the resources necessary to finance reforms in the electricity and telecommunications sectors.

III. THE PROJECT

A. Objectives

- 3.1 The MIF financing is intended to fund the activities necessary for attracting technical and operating capacity, and for mobilizing private sector financing and resources for the provision and expansion of civil aviation services.
- 3.2 The proceeds of the Bank's technical cooperation loan will be used to strengthen the capacity of the Directorate of Civil Aviation as an administration, oversight and regulatory agency for the contracts with the private sector. The Bank resources will also be

used to develop the subcomponent comprising private sector participation in the air traffic control systems.

B. Proposed strategy

- 3.3 The design of the proposed privatization transaction includes the following elements: (i) a long-term concession for the operation, exploitation and development of La Aurora Airport that will probably include the San José and Santa Elena Airports as well; (ii) the transfer of responsibilities to the private sector includes all activities (aeronautical and commercial) from the moment an aircraft reaches the terminal (point of embarkation, access door or tunnel) to the moment that the aircraft with passengers/freight on board leaves the terminal; (iii) the concession includes investment commitments on the part of the concession holder for developing the airport infrastructure and serving increased demand in accordance with international standards; (iv) presence of an international airport operator in the consortium; and (v) the concession would be awarded through an international competitive bidding process.

C. Description of products and activities

1. With MIF financing

- 3.4 To finance the *private sector participation in air transportation infrastructure* component, the MIF resources will be used to hire three consulting firms that will be responsible for preparing the following outputs: (i) the investment plan (specifying the investment and expansion needs during the concession period); (ii) the economic and financial analysis of the concession; (iii) the design of the transaction; (iv) the preparation of the sale memorandum; and (v) the concession contract.
- 3.5 The air transportation consultants will prepare the master plan and the investment plan for the sector, the economic analysis, and the financial evaluation of the possible scenarios for development of the concession. The main outputs of this consulting process would be the following: (i) the model for estimating demand (analysis of passenger and freight traffic); (ii) the investment plan; (iii) the financial simulation model (analysis of tariff consistency and airport fees, the investment plan, traffic volumes, etc.); and (iv) the proposal for formulating the airport tariffs and fees policy. Working with the legal and financial advisory firms, the database necessary for designing the transaction, preparing the sales memorandum, and negotiating and awarding the concession contract will be developed.
- 3.6 The legal advisory firm will be responsible for: (i) a legal audit of the assets and liabilities in respect of the prospective concession; (ii) developing and preparing, in cooperation with the

financial advisory firm, the documentation necessary for the concession contract, and proposing and designing the legal configuration of the transaction; (iii) with the support of the financial advisory firm, preparing the tender documents (including the investment plan for the first five years, concession rights payments, etc.); (iv) advising the government (CEDE and MCTOP), during the bidding, selection, negotiation, award and conclusion of the transaction. Notwithstanding the provisions the annex to the agreement concerning the selection and contracting of consulting firms and experts, it will not be necessary to obtain the Bank's approval with regard to the concession contract negotiated to effect the final payment to the legal advisory firm.

- 3.7 The financial advisory firm, with the cooperation of the legal advisor and the advisor on air transportation, will be responsible for: (i) preparing the sales memorandum; (ii) the "road show" marketing of the investment opportunity; (iii) preparing the tender documents to be used in the bidding process; (iv) the bidding process; (v) proposing the system for qualifying, evaluating and selecting bids; and (vi) conclusion of the negotiations.
- 3.8 The preparation of the master plan, including the investment plan and the financial simulation model, should be completed within four to five months. By that date the legal and financial advisory firms will already have started their work. In the second six-month period the alternatives for the concession would be evaluated, the transaction designed and the sales memorandum prepared. It is proposed that in the first quarter of 1998 the strategic private investor for the concession be selected and the pertinent negotiations conducted. It is expected that the concession will be granted in the first half of 1998.

2. With financing from the technical cooperation loan

- 3.9 To finance the *institutional strengthening* component, the resources of the Bank's technical cooperation loan will be used to fund the following outputs and activities: (i) design of the new organization of the current DGAC (regulatory and oversight agency for the contracts with the private sector), including the preparation of operating and procedures manuals, the proposed job descriptions and salary structure, and the management information systems; (ii) adaptation of technical rules and procedures to comply with ICAO standards, including preparation of the technical regulation manuals; (iii) training and development for the DGAC's management and technical staff; and (iv) procurement of the equipment and information systems.
- 3.10 To finance the *private sector participation in air traffic control* component, the funds from the technical cooperation loan will be used to finance preparation of the investment plan, the evaluation of the economic and financial feasibility of participation by the

private sector in service delivery, financing and expansion of the systems, and possibly the preparation of the bidding documents for a contract with the private sector. In order to provide technical support to the civil aviation technical unit, the resources will be used to hire experts in programs to incorporate the private sector into airport operation.

IV. COST AND FINANCING

- 4.1 The total cost of the program for which technical cooperation support is to be provided is US\$3.85 million, broken down as shown in Table I below. The MIF would contribute a total of US\$1.15 million in the form of a grant, the Bank would provide US\$1.8 million (OC), and the government would contribute counterpart resources equivalent to around US\$900,000.

TABLE I
SECTOR REFORM AND PRIVATE SECTOR PARTICIPATION IN CIVIL AVIATION
(in US\$ thousands)

	COMPONENTS	IDB (OC)	MIF	LOCAL	TOTAL
A.	INSTITUTIONAL STRENGTHENING	900		300	1,200
B.	PRIVATE SECTOR INVOLVEMENT	450	1,150	550	2,150
1.	Airports	200	1,150	500	1,850
1.1	Air transport advisor ^{1/}		450	150	600
1.2	Legal advisor		400	100	500
1.3	Financial advisor		300	100	400
1.4	CEDE ^{2/}	200		150	350
2.	Air Traffic Control	250		50	300
C.	ENVIRONMENTAL CONSERVATION	150		50	200
D.	CONTINGENCIES	150			150
E.	INSPECTION AND SUPERVISION	150			150
	TOTAL	1,800	1,150	900	3,850

^{1/} Short lists compiled by direct invitation.

^{2/} Includes the expenditures of the Directorate of Civil Aviation and the Special Divestiture Committees of the Office of the Commissioner for the Modernization of the Executive Branch.

V. EXECUTION AND DISBURSEMENT

- 5.1 The execution and administration of the project will be performed using the same arrangements as set up for the Bank's technical cooperation. The contracting of advisory services will be done by the project coordination unit (PCU), with UNDP assistance, in accordance with the relevant Bank and MIF procedures.
- 5.2 Since there is only a small number of specialized firms eligible for the air transportation advisory services component, it is proposed that the limited international bidding procedure, as set forth in the *Basic Procurement Policies and Procedures of the IDB*, be followed. Under this method, **participation in the bidding is by express invitation rather than a public announcement**; that is, there is no need for publication in *Development Business*.
- 5.3 For the selection of consulting services, **the lowest bid method of selection will be used**. Under this method, technical and economic bids are presented in two separate envelopes, and a "minimum acceptable technical level" is established for assessing the technical bids. The technical bids are opened first and evaluated. Bids that do not meet the minimum acceptable level are rejected and only the economic bids of the remaining bidders are opened. The firm with the lowest bid is then selected. The minimum level will be explicitly indicated in the requests for proposals.
- 5.4 An execution period of 24 months is proposed, and the grant funds will be disbursed over a period of 30 months.

VI. COMPLIANCE WITH ELIGIBILITY REQUIREMENTS

- 6.1 The technical cooperation project, designed to support the modernization efforts and private participation in the infrastructure sector, is fully compatible with the MIF's general objective, namely strengthening of private investment and its expansion, thereby speeding the country's economic growth and social development.
- 6.2 The proposal is compatible with Article 3, Section 2 (c) and (d) of the Agreement Establishing the MIF, which provides for grants from the Technical Cooperation Facility to governments for advisory services to establish and/or strengthen regulatory agencies. The proposal is also consistent with the recent recommendations of the MIF Working Group to support development of the legal, regulatory, contractual, and supervisory framework to give priority to the promotion of private investment in the infrastructure and public service sector.

VII. CONSISTENCY WITH THE BANK'S COUNTRY PROGRAM

- 7.1 This financing complements the support being provided by the Bank to the Government of Guatemala for the reform of basic infrastructure sectors. This operation is an integral part of that effort, and is considered essential to promote private sector participation in these sectors.

DEVELOPMENT INDICATORS
A-V.1 TELECOMMUNICATIONS

INDICATORS	DEFINITION	PRESENT LEVEL
ing (%)	(Private financing/Total financing) * 100	14%
ment rate (%)	(Average annual investment executed/Investment necessary) *100	20%
ional long distance	Rates/Economic efficiency rates	1.0
		1.0
	Lines per 100 inhabitants	3.8
	Public telephones per 100 inhabitants	0.04
	Public telephones in communities with fewer than 300 inhabitants	0.0
ding for telephone service (ratio)	Requests pending/Telephone lines in services	3.1
ed from telephone exchanges in local traffic (%)	(Calls completed per month/Calls attempted per month) *100	41.5
omatic international calls completed (%)	(Calls answered per month/Calls attempted per month) *100	41.7
omatic international calls completed (%)	(Calls completed per month/Calls attempted per month) *100	52.0
per employee	Employees per 1,000 lines	28

A-V.2 ELECTRICITY SECTOR

INDICATORS	DEFINITION	PRESENT LEVEL
ing (%)	(Private financing/Total financing) *100	17%
ment rate (US\$ million/year)	Investment effected annually	14.5
	Tariffs/Economic efficiency tariffs	97%
	(Population with house connection/Total population)*100	51%
ability (%)	(Hours with equipment available/24)*100	70-90%
bility (%)	(Hours with equipment available/24)*100	86-90%
ty losses (%)	(1-Energy billed/Energy generated)*100	11.7%
per employee	MWh/employee	508

A-V.3 CIVIL AVIATION ^{1/}

INDICATOR	DEFINITION	PRESENT LEVEL
and rehabilitation of existing La Aurora Airport		
mic indicators	Savings in public budget (funds allocated to the General Directorate of Civil Aviation)	n.a.
cy and productivity indicators	Greater aircraft and passenger handling capacity	n.a.
	Expected increase in traffic	n.a.
	Improvements in user service indexes (passengers and airlines)	n.a.
construction of new airport (Guatemala City)		
mic indicators	Savings in public budget (funds allocated to the General Directorate of Civil Aviation)	n.a.
mental impact indicators	Improvements in average (per m ³) pollution in Guatemala City (aircraft engines, pollution and decibels)	n.a.
indicators of flight safety and protection	Improvements in flight safety indexes at aircraft approach and takeoff.	n.a.
ts and rehabilitation of the rest of the system		
cy and productivity indicators	Integration of cities and regions with the main airport. Connection with the rest of the world.	n.a.
	Improvements in user service indexes (passengers and airlines)	n.a.

not available

lack of data on the present situation reflects the institutional weakness of the DGAC. The database will be developed by the firm providing advisory services on air transport preparation of the concession contract.

PROPOSED RESOLUTION

GUATEMALA. LOAN ____/OC-GU TO THE REPUBLICA DE GUATEMALA
(Sectorial Program for Investment and Infrastructure Sector Reform)

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 República de Guatemala, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a Sectorial Program for Investment and Infrastructure Sector Reform. Such financing will be for the amount of up to US\$100,000,000, which are part of the resources of the Single Currency Facility of the Ordinary Capital of the Bank, and will be subject to the "Special Contractual Conditions" and the "Terms and Financial Conditions" of the Executive Summary of the Loan Proposal.

PROPOSED RESOLUTION

GUATEMALA. TECHNICAL COOPERATION LOAN TO SUPPORT THE
SECTORIAL PROGRAM FOR INVESTMENT AND INFRASTRUCTURE SECTOR REFORM

The Board of Executive Directors

RESOLVES:

1. 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 agreements as may be necessary with the República de Guatemala and to adopt such measures as may be pertinent for the execution of the plan of operations with respect to a Technical Cooperation Loan to Support the Sectorial Program for Investment and Infraestructure Sector Reform, referred to in Document PR-_____.

2. That up to the sum of US\$7,650,000, is authorized for the purposes of this resolution, chargeable to the resources of the Single Currency Facility of the Ordinary Capital of the Bank.

3. That the above-mentioned sum is to be provided on a reimbursable basis.