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Report No: 27420

IMPLEMENTATION COMPLETION REPORT
(TF-26673 FSLT-70920)

ON A

LOAN

IN THE AMOUNT OF US$400 MILLION

TO THE REPUBLIC OF

COLOMBIA

FOR

STRUCTURAL FISCAL ADJUSTMENT

DECEMBER 5, 2003

CURRENCY EQUIVALENTS

(Exchange Rate Effective December 5, 2003)

Currency Unit	=	Peso
MXP$ 11.410	=	US$ 1
US$ 0.0876	=	MXP$ 1

FISCAL YEAR

January 1 December 31

ABBREVIATIONS AND ACRONYMS

Vice President:	David de Ferranti
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COLOMBIA
CO Structural Fiscal Adjustment Loan

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Project ID: P073572	*Project Name:* CO Structural Fiscal Adjustment Loan
Team Leader: David Michael Gould	*TL Unit:* LCSPE
ICR Type: Core ICR	*Report Date: December 29, 2003*

1. Project Data

Name:	CO Structural Fiscal Adjustment Loan	*L/C/TF Number:*	TF-26673; FSLT-70920
Country/Department:	COLOMBIA	*Region:*	Latin America and the Caribbean Region

Sector/subsector: Sub-national government administration (32%); Central government administration (26%); Compulsory pension and unemployment insurance (16%); Health (16%); Health insurance (10%)

Theme: Public expenditure, financial management and procurement (P); Other economic management (P); Other public sector governance (S); Health system performance (S); Tax policy and administration (S)

KEY DATES			Original	Revised/Actual
PCD:	09/17/2001	*Effective:*	12/20/2001	
Appraisal:	11/02/2001	*MTR:*		
Approval:	12/18/2001	*Closing:*	02/21/2003	

Borrower/Implementing Agency: GOVERNMENT OF COLOMBIA/MINISTRY OF FINANCE

Other Partners:

STAFF	Current	At Appraisal
Vice President:	David de Ferranti	David de Ferranti
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2. Principal Performance Ratings

(HS=Highly Satisfactory, S=Satisfactory, U=Unsatisfactory, HL=Highly Likely, L=Likely, UN=Unlikely, HUN=Highly Unlikely, HU=Highly Unsatisfactory, H=High, SU=Substantial, M=Modest, N=Negligible)

Outcome: S

Sustainability: L

Institutional Development Impact: M

Bank Performance: S

Borrower Performance: S

	QAG (if available)	ICR
Quality at Entry:		S
Project at Risk at Any Time:	No	

There is no Quality at Entry Report available for this project

3. Assessment of Development Objective and Design, and of Quality at Entry

3.1 Original Objective:

Introduction

Colombia's fiscal situation deteriorated noticeably in the mid-1990s, characterized by both significant deficits and the creation of large future liabilities. The primary causes of this situation were structural in nature and reflected the rapid expansion of the public sector and an increase in pension liabilities. Despite increased public sector spending, the government of Colombia could not respond to mounting social demands to provide essential services, most importantly in the realm of peace and security. The problem was compounded by structural rigidities in the tax and public expenditure systems that made it difficult to allocate scarce resources in an efficient and effective manner. Such a restricted fiscal position made Colombia particularly vulnerable and ill prepared to respond to the sharp economic recession that unfolded after 1998. Today, Colombia's economic situation shows tentative signs of growth and the fiscal situation, while still vulnerable, has shown sustained signs of improvement. Colombia's rate of economic growth has turned from a 4.2 percent decline in 1999, to 1.7 percent growth in 2002 and may reach as much as 3 percent growth this year. Moreover, the non-financial public sector deficit has fallen from 6.2 percent of GDP in 1999 to around 4 percent in 2002.

The SFAL assisted the government in two important ways. First, it helped the government to begin a process of slowing the growth of fiscal imbalances. The proceeds from the loan helped to reduce the cost of borrowing and to lengthen the debt maturity by providing a confidence-building signal to international markets, all of which gave the government fiscal space for protecting social sector expenditures and implementing difficult structural measures. Second, the SFAL promoted reforms in the provision of public services that improved incentive structures and provided substantial efficiency gains. As a result, the fiscal rigidities facing the Colombian government were reduced and the fiscal situation is gradually stabilizing—important first steps in putting Colombia on a sustainable fiscal path.

As recognized in the SFAL initiating documents, the loan was not without significant risk, especially considering that the program would be implemented over two different presidential administrations. But despite the risk undertaken, there was a tangible payoff to the program. While many of the reforms promoted by the SFAL are still only in their initial stages of implementation, the SFAL provided an important impetus to the government's reform program. Without support from the Bank it is doubtful that these reforms would have progressed as they have. Nonetheless, fiscal sustainability has not yet been achieved and further support for these reforms to ensure long-term sustainability is critical. Ongoing support is being provided by the Bank through a continuing program of Fiscal Institutional Adjustment Loans (FIALs) as well as other adjustment programs. However, the fiscal situation is still difficult as evidenced by a recent constitutional court ruling against a planed increase in the value-added tax, higher than expected military expenditure, and the failure to garner enough votes for the passage of an important fiscal adjustment referendum. Although a "Plan B" has been formulated by the government as an alternative to the referendum that can be implemented by executive decree, the near-term trajectory remains uncertain.

Original objective

The overall objective of the operation was to support the government's commitment to improve Colombia's fiscal accounts and implement structural fiscal reforms, an essential first step toward reaching full fiscal sustainability, sustaining high economic growth and achieving poverty reduction. The program focused on a core set of policies that strengthen the country's fiscal outlook. This policy package included: (a) rationalizing the system of transfers to local governments, and imposing more market-driven and more binding budget constraints on their finances; (b) establishing mechanisms to arrest the exploding cost of inefficiency in the provision of public health services; (c) halting the accumulation of pension-related contingent liabilities; (d) advancing the reorganization of public agencies and their current expenditures; and (e) setting up a better system for managing public debt.

The components of the loan presented a package of reforms aimed at addressing the structural rigidities in Colombia's fiscal accounts. The loan was viewed as responsive to the borrower's circumstances in the light of fiscal rigidities that remain a key constraint to effective public policy in Colombia. It is also viewed as responsive to the borrower's development priorities given that it sought to promote a reform agenda identified and developed by the government itself.

While the number of policy and institutional reforms was high, the program was not overly complex and the domestic commitment to the reform agenda meant that the goals of the loan were realistic and achievable.

3.2 Revised Objective:
The Objective was not revised

3.3 Original Components:
The FSAL supported a fiscal reform program that addressed six key areas with the aim of meeting the objectives described above. The Bank's financial support was programmed for disbursement in three tranches over a 14-month period with the disbursement of each tranche being tied to advances in the implementation of the fiscal reform program, including the meeting of certain key indicators (details of the conditions are provided in Annex A).

<u>Component 1: Macroeconomic framework;</u>

- Maintain a macroeconomic framework consistent with the objectives of the program.

<u>Component 2: Intergovernmental fiscal relations;</u>

- Implement a reform of the fiscal transfer system from the central government to subnationals, limiting the rate of growth of fiscal transfers and the rate of growth of the central administration operational expenditures for 2002 and thereafter.

- Reform the tax system of territorial entities (*Estatuto de Ingresos Territoriales*) to increase subnational tax revenues by more than 20% in its first year of application.

- Issue and implement a decree to regulate debt and borrowing of territorial entities that will contribute to halting unsustainable borrowing, limiting bailouts, and eliminating discretionality in the treatment of debt.

<u>Component 3: Health</u>

- Approve a national public hospital restructuring policy and implementation program, including the selection of at least ten departments and covering more than 15 percent of the FY01 public hospital budget.

- Sign contracts with at least three subnational governments to finance the restructuring of public hospitals, including specific targets for labor cost reductions and productivity increases.

- Transform at least 60% of the *situado fiscal* in FY01 (after legal mandatory deductions) to demand subsidies.

Component 4: Reform of the Social Security Institute (ISS)

- Implement a restructuring plan for ISS that will make it financially and economically viable, including negotiations with ISS unions about labor costs and benefits, debt restructuring including renegotiating 50% or more of ISS debt, and the reduction of at least 30% in the waiting list for elective surgeries.

Component 5: Pension

- Create a new social security department in the Ministry of Finance for improving social security system control that should generate substantial fiscal savings.

- Congressional approval of a new law to reform the general pension system with the aim of putting it on a sustainable fiscal path or a law to reform at least one of the exempted pension regimes to bring them in line with the general pension regime.

Component 6: Public Sector Reform

- Reduction in total central government current expenditure in the government's approved budget for FY02 of more than 4 percent in real terms. Actual expenditure should not exceed these levels.

- Reduction in central government's general expenditures of more than 15 percent in real terms in the government's approved budget for FY02 in relation to the same expenditures in the FY00 executed budget. These expenditures should be no higher in real terms than spending incurred in FY01.

Component 7: Education

- Amendment of the law to provide for certification of municipalities that represent at least 40 percent of the country's school enrollment enabling such municipalities to autonomously manage the provision of education services (including teacher payroll) and to establish education performance monitoring mechanisms; or (b) certification of municipalities that represent at least 14 percent of the country's school enrollment enabling such municipalities to autonomously manage the provision of education services (including teacher payroll) and intergovernmental performance agreements have been signed between the Central Government and such certified districts and municipalities. In either case, no extra budgetary transfers for education to certified districts or municipalities have taken place.

3.4 Revised Components:

The components were revised, but not substantially. A partial waiver was sought for release of the "floating tranche" relating to the commitment to approve the new subnational tax law (*Estatuto de Ingresos Territoriales*, component 2, part 2 above). Although the law that was passed did not contain the exact measures envisaged in the draft law submitted to Congress, it complied with the overall goal of increasing subnational revenue. Nonetheless, the revision of this component did factor into the overall rating of the program.

3.5 Quality at Entry:

Quality at entry is rated *satisfactory* based on: (i) consistency of objectives of the loan with the government of Colombia's reform agenda and therefore, (ii) strong ownership of the program on behalf of the government, (iii) demonstrated capacity of the implementing agency, and (iv) adequate project design that correctly identified risks and mitigating factors. The country assistance update note issued on November 16, 2001 considered the adjustment loan operation as a way to support fiscal reforms and Colombia's ongoing efforts in this area.

Overall, the components described above were adequately designed for meeting the general objectives of the loan (i.e., beginning the process of putting the fiscal accounts on a sustainable trajectory). Partnership with the IMF in monitoring and supporting the macroeconomic environment was extremely helpful during a period of particularly turbulent external economic conditions and domestic security concerns. The components of the loan took into account the capacity of the implementing agencies and the lending instrument itself was appropriate for the objective. The design of the lending program, which included two scheduled tranches and final floating tranche, allowed for sufficient flexibility to accommodate the uncertain timing in the completion of the final conditions of the loan (particularly the congressional approval of territorial tax reforms).

With the benefit of hindsight, the restructuring of the Social Security Institute (ISS) would likely have benefited from a longer-term strategy to boost management and implementation capacity during the loan period to ensure success. Restructuring of the ISS has lagged other reforms due to, in part, strong vested interests, but also to a lack of a clear strategy for reform. To address this problem, the management of the ISS is currently formulating a strategy for further reform, but much work still needs to be done.

In addition, a slower disbursing programmatic loan, utilizing executed budget figures rather than initial approved budget figures, would have proved a more accurate monitoring indicator for judging fiscal stance, but the programmatic approach was not available at the start of the SFAL. The relatively short period between disbursements required monitoring indicators based on partial and preliminary assessments of budget outlays and not final outcomes. The trade-off, of course, is that waiting for final budget figures would have substantially delayed the country's much needed access to funds.

4. Achievement of Objective and Outputs

4.1 Outcome/achievement of objective:

Outcome is assessed as *satisfactory*

The SFAL proved to be an important element in ensuring the continuity of fiscal reform during the political transition in Colombia. While the loan was approved and the first tranche released during the Pastrana administration, the new Uribe government demonstrated a solid commitment to continuing fiscal reform through the SFAL and fulfilled the requirements for disbursement of the second and floating tranches of the loan.

The program achieved many of its immediate goals as set out in the conditions for tranche release. This initiated a series of reforms that in the medium-term will produce further improvement towards fiscal sustainability and the provision of services. While the SFAL took initial steps to restrain growth in spending and reduce moral hazard with regards to subnational governments and decentralized social security institutions, needed supplementary measures to effectively reduce budgetary entitlements are being pursued in subsequent projects. Similarly, the SFAL took important steps towards institutionalizing a system of inter-governmental fiscal agreements for the provision of education services that will also take several years to bear significant results. Although it is too early to determine if the program had a measurable impact on trend economic growth or poverty, it likely helped the country weather an extremely volatile external environment by reducing market concerns over the sustainability of its fiscal imbalances. Many of the reforms initiated under the SFAL have been continued with the support of the Bank through the Fiscal and Institutional Adjustment Loans (FIAL I and II) and through the Labor and Social Structural Adjustment Loan.

4.2 Outputs by components:

Component 1: Macroeconomic framework; This element is rated *satisfactory*

During the program period Colombia encountered several economic challenges. It faced issues of contagion resulting from economic problems in Venezuela, the largest market for Colombia's nontraditional exports; the worsening of market sentiment toward Latin America; and slow economic recovery in the United States, Colombia's main trading partner. Internally it faced increasing security costs at the same time as it was undergoing a political transition. In light of these issues and its efforts to maintain a stable economy, despite a significant deterioration in its fiscal deficit in 2002, the macroeconomic framework is evaluated as having been consistent with the objectives of the program.

Fiscal performance improved markedly between 1999 and 2001, but the public sector finances weakened in 2002. When the Uribe administration took office in August 2002, the deficit of the combined non-financial public sector risked rising to nearly twice the target of 2.6 percent of GDP under the IMF's Extended Fund Facility (which started in 1999). The fiscal slippage reflected increased military spending, a revenue shortfall on account of lower-than-expected economic growth and spending commitments made by the previous administration. Economic activity in 2002 was sluggish (real GDP growth was about 1.6%) and inflation remained subdued (7% year-on-year). International reserves increased in 2002 and there was no major central bank intervention to support the currency, which depreciated in nominal terms against the US dollar. Due to weak demand for imports and the domestic currency depreciation, the current account deficit fell to about 1.8% of GDP in 2002 from 2.5% of GDP in 2001.

Faced with the fiscal challenges, the new government took steps to rein in the budget deficit. First, it levied a one-off tax on net wealth to finance the effort to take control of the security situation. Second, in December 2002, it presented and won approval by Congress for a policy package containing both temporary and permanent taxation measures. While the deficit ultimately rose to 4.1 percent of GDP in 2002, it was less than what may have occurred had the new administration not acted decisively when it did.

Following the actions of the government to reign in the deficit, in January 2003, the IMF board approved a two-year SDR 1.5 billion Stand-by arrangement in support of Colombia's economic program. The government has successfully completed reviews under the recent stand-by arrangement with the IMF up through the end of March 2003. While the failure of October's referendum on fiscal reforms has raised questions about the country's ability to meet its fiscal targets under the IMF program, the government has been working on implementing an alternative strategy (with support from the Bank and the IMF) to achieve similar results.

Component 2: Intergovernmental fiscal relations; This element is rated *satisfactory*.

The government committed to implement a reform of the fiscal transfer system from the central government to subnationals, limiting the rate of growth of fiscal transfers and the rate of growth of the central administration operational expenditures. The Constitutional reform of 2001 combined the three major sources of transfer financing into the *Sistema General de Participaciones*. Within this reformed framework, the government explicitly prohibited the distribution of any cash transfers to subnational governments except where the distribution is specified by formula or law. On the expenditure side, the constitutional reform limited the rate of growth of total transfers to subnational governments to last year's inflation plus 2 percent and limited the growth of central operational expenditures to inflation plus 1.5 percent. To help control general administration costs, subnational governments received structural adjustment loans to finance downsizing of personnel. The government also committed to regulate subnational debt, and in accordance with Law 617 of 2000, since July 2001, the central government has not provided bailouts to territorial entities or guarantees on their debt. Further, it linked borrowing by subnational entities with the rating of two international credit rating agencies and restricted commercial borrowing for all entities having loans subsidized under Law 617 of 2000.

The commitment to reform the tax system of territorial entities (*Estatuto de Ingresos Territoriales*) to increase subnational tax revenues by more than 20%, was substantially met by the passing of Law 788-2002, which is projected to raise subnational revenues by the stipulated margin in 2003 and is on its way to doing so. The measure of greatest fiscal importance in the draft law submitted in 2001 was the rationalization of alcoholic beverages taxes that was included in Law 788-2002 along with measures to establish rates and rules for setting gasoline taxes, norms on the taxable value of mortgages and open collaterals and the use of public-private systems for collecting registry taxes, and norms on tax procedures for departments and municipalities. In regard to this law, a waiver was sought for the release of the floating tranche given that the draft law was not approved in its original form. However, as mentioned above (section 3.4), the final version of the law contained most of the intended results of the proposed reforms and had the effect of increasing subnational revenue by more than 20%.

Component 3: Health sector; This component is rated *satisfactory*

The government's main commitments with respect to health services were to (a) reduce inefficient supply-side subsidies; and (b) limit the fiscal costs to the national government while improving service. Under the SFAL, the government implemented a National Hospital Restructuring Policy. The pilot phase of the program in 2002 covered more than 10 departments and 15% of the total hospital budget. The program included specific targets for cost reduction and productivity increases which generated more than 5% in fiscal savings per month. The government also completed its commitments to transform over 60% of the *situado fiscal* from supply subsidies to demand subsides.

Component 4: ISS Reform; This component is rated *unsatisfactory*

The government implemented a restructuring plan although it did not achieve its goal of putting the ISS on a financially and economically viable path. The specific measures implemented included renegotiating special-benefit agreements with the labor unions, restructuring the ISS debt, improving its financial management, eliminating 8,000 vacant positions, and closing ambulatory health facilities. The government still plans to restructure the provision of direct health services and reduce the operation of the ISS to make it consistent with current and future demand and the possibility of closing the ISS if the reform process is not successful is still an option. It is clear that further reform and sustained capacity building will be needed if ISS is to become a viable organization.

Component 5: Pension; This element is rated *satisfactory*

The government created the Social Security Economic Regulation Agency (Dirección de Regulación Económica de la Seguridad Social, DRESS) to serve as a counterpart and advisor to the Ministry of Social Protection (Ministerio de Protección Social, MPS) in managing and tracking pension and social security expenditures. Ongoing controls and enhanced administration have generated significant fiscal savings in the areas of pensions, health, and workers compensation (estimated at US $300 million in 2001). The activities of DRESS include the tracking, validation, calculation of actuarial pension benefits, and pension payments of the National Public Pension Fund (Fondo de Pensiones Públicas del Nivel Nacional, FOPEP). The Congress also passed a pension reform law in December 2002 reducing the use of exempted pension systems, explicitly bringing ECOPETROL workers into the general pension system and reforms have subsequently been made to the pensions of teachers and security forces. The law also approved reforms that allow for a gradual increase in the rate of contributions during 2004-2006 by 2%, a reduction in the replacement ratio and a gradual increase in the contribution period from 1000 weeks to 1300 weeks by 2015. With these reforms in place new entrants into the system will not generate increases in the actuarial deficit, although this deficit still exists and further reform or financing is required to overcome this.

Component 6: Public Sector Reform; This element is rated *marginally satisfactory*

The government undertook several commitments to reduce and rationalize government spending. It promised to reduce by more than 4 percent in real terms the approved budget for central government current expenditure as compared with the budget approved in FY2001 and then limit actual spending to these levels. The approved budget complied with these restrictions (as did spending levels at the time of the second tranche release in 2002). However, final spending by year end represented a 4 % increase over FY2001 spending levels in real terms.

With regard to the restrictions the government committed itself to in the area of general expenditure (*gastos generales*), the government came close to its initial commitment to reduce these line item appropriations by 15% in real terms as compared with that spent in the same areas in FY2000. Although it fulfilled the commitment requiring that FY2002 budgeted amounts to be lower than FY01 spending, actual spending in real terms by year end was higher than that executed during FY2001. The approved budget included reductions in this area of 19% in real terms, but by year end actual spending represented an increase of 16% over FY2001 actual expenditure.

The results indicate the tendency for actual spending to differ significantly from that approved at the start of the year. This would suggest that it would be valuable to review the use of conditionality based on budget appropriations (as opposed to executed budget) if the goal is actual, rather than planned, fiscal adjustment. The evidence of a further fiscal slippage since the end of the SFAL implies that unless monitoring is ongoing, real sustained fiscal adjustment may be difficult to achieve through quick disbursing loans.

Component 7: Education; This element is rated *satisfactory*

With the passing of Law 715 of 2001, the government amended the existing law, allowing for certification for management of the provision of education services. The law allowed all municipalities that are capitals of departments or have a population of more than 100,000 inhabitants to receive certification which represented more than 40 percent of the country's school enrollment. Performance monitoring mechanisms were also established with these municipalities to monitor quality of service provision. No extra budgetary transfers were undertaken to these municipalities.

4.3 Net Present Value/Economic rate of return:
It was not possible to calculate net present value or economic rate of return.

4.4 Financial rate of return:
It was not possible to calculate a financial rate of return for this project.

4.5 Institutional development impact:
The Institutional Development (ID) impact of the SFAL is rated as *moderately high*. The conditions set forth in the SFAL generated incentives for decentralization as well as a framework for efficiency gains in the provision of health services and insurance and education, controls on new pension obligations, and limits on sub-national borrowing. Although the institutions addressed in the program are still not fiscally sustainable (for example, the ISS and the pension system), the initiatives developed created an environment for long-term institutional development that is being carried forward in the current programmatic Fiscal and Institutional Adjustment Loans (FIAL). Without the first steps taken under the support of the SFAL, it would be difficult to envisage the progress made to date.

One particularly important institutional development was the creation of a new agency (Dirección de Regulación Económica de la Seguridad Social, DRESS) in the Ministry of Finance and Public Credit for control and tracking of social security benefits and pension obligations. Prior to the new agency's creation, there was no central control or oversight of general pension obligations or uniformity in rules and policies, which led to a growing list of ineligible pension claims. The lack of a unified and consistent treatment of pension obligations, compounded by high turnover among government workers administering the multitude of public pension regimes, led to a burgeoning of non-conforming pension liabilities. With the creation of a single oversight agency within the Ministry of Finance, ongoing savings of more than US$10 million per month are being generated.

The program to restructure and better manage public hospitals has also generated substantial savings and efficiency gains among the initial 26 public hospitals in the program. It has also helped to refine the process for restructuring the remaining hospitals in the public health system. Nonetheless, only a small faction of the public health system has been restructured and much remains to be done, particularly in ISS. A problem with the SFAL, especially in relation to the objective of putting the ISS on a financially and economically sustainable path, was that it did not link development objectives with a long-term strategy in reforming (or dismantling) complex institutional structures with strong entrenched vested interests. For example, programs that may have had the objective of reducing costs by eliminating redundant personnel, did not follow through with long-term incentives to prevent the re-hiring of personnel to keep future spending lower. The difficulties in restructuring the ISS may have been inevitable, but a long-term strategy to address potential problems and incentives would have likely created a more sustainable reform.

5. Major Factors Affecting Implementation and Outcome

5.1 Factors outside the control of government or implementing agency:
The external economic environment for Colombia was extremely difficult during the implementation period of the SFAL, which makes the country's achievements under the program that much more impressive. Not only was the global economy suffering from a sharp deterioration in growth and heightened uncertainty due to the terrorist attacks of September 11, 2001, but the relative prices of Colombia's primary exports (coffee

and oil) deteriorated significantly during this period. Moreover, increased internal violence and the uncertainty over its resolution, contributed to widening credit spreads and increased borrowing costs. Venezuela, an important export market and neighboring country, also suffered from political and economic crisis that had negative effects on Colombia. As a result, Colombia's traditional exports fell by over one-fourth and real GDP grew only about 1.5 percent, on average, between 2001 and 2002. The weak external environment and consequent domestic slowdown worsened the already fragile fiscal situation.

5.2 Factors generally subject to government control:
Despite the difficult external economic environment, the Colombian government maintained a sound macroeconomic framework throughout the implementation period of the SFAL in accordance with the project conditionality, and this was crucial to support the institutional reforms taking place at the national and sub-national level. Subdued price pressures allowed the Central Bank to reduce interest rates, which, along with enhanced prudential regulation, helped the financial sector rebound from the crisis of 1998-1999. The commitment of high-level government authorities to structural and fiscal reform was strong and this helped facilitate the implementation of the program.

5.3 Factors generally subject to implementing agency control:
The Ministry of Finance and Public Credit had the primary responsibilities for implementing the SFAL. All conditions of the SFAL were met with the support of the Ministry of Finance and Public Credit, except for part of the last condition in the final tranche of the loan. This last condition in the final "floating" tranche included the requirement that Congress pass a particular law to reform the tax system of the territories. Instead of passing the original draft of the law, a variant of the law was passed that had the same, if not greater, fiscal savings and distributional impact but did not include the specific increases and standardization of sources of income for territories that had appeared in the original draft law. Taking a pragmatic approach to the political realities at the time (a large set reforms were passed by Congress earlier in the same month) the Uribe administration and the Ministry of Finance felt that a slightly different law (with similar objectives) was more politically feasible. Nonetheless, this figured negatively into the assessed impact of the program.

5.4 Costs and financing:
There were no cost changes.

6. Sustainability

6.1 Rationale for sustainability rating:

Sustainability is considered *likely* although the speed of adjustment to fiscal balance will probably be slower than originally anticipated. The structural reforms undertaken during program implementation have been continued since completion of the project reflecting the government's commitment to the reform agenda. This is particularly true in the area of inter-governmental fiscal relations where progress was critical for program success and indeed has been notable. The initial reforms undertaken in the health and education sectors have been successful and promise both improved service and reduced fiscal burden for the states.

But fiscal sustainability requires that these reforms be implemented on a wider scale. Further reform is still needed in the areas of social security and pensions to ensure that the programs offered will provide ongoing coverage. Despite the government's strong commitment to correcting the fiscal imbalances, obstacles have appeared that have partially thwarted the government's best efforts. A proposed 2 percent value-added tax on previously exempted consumer goods was ruled unconstitutional by the courts in September 2003 and a referendum including fiscal and political reforms failed to garner the required 25 percent of the electorate (although over 80 percent of those voting were in favor of the referendum) in late-October 2003. While these setbacks are have slowed progress in reducing the fiscal imbalances, the government is pursuing alternative measures to reduce the deficit.

6.2 Transition arrangement to regular operations:

The government is continuing its reform program, particularly in the areas relating to fiscal rigidities through a series of Programmatic Fiscal and Institutional Structural Adjustment Loans (FIALs) with the Bank. In addition, the Bank is working closely with the Inter-America Development Bank in its overall reform assistance and in specific program areas of asset management, legal defense of the state, and information technology. Colombia's macroeconomic framework continues to be supported and monitored closely under the IMF Stand-by loan agreement.

7. Bank and Borrower Performance

Bank

7.1 Lending:

The Bank's overall performance in lending was *satisfactory*. In response to the Colombian government's request for assistance in helping to correct its structural fiscal imbalances, the Bank assembled a team of specialists to assist the country in formulating proposals for fiscal strengthening. The country was also assisted by the IMF in developing a stable macroeconomic framework for reform under a three-year Extended Arrangement Facility (begun in December 1999) and also had a close partnership with the IDB in adjustment operations in the financial and electricity sectors as well as in assistance to the social safety net program. The Bank team worked closely with the government authorities in developing their fiscal program and provided analytical support to the government in evaluating the relative short-term economic costs versus the long-run benefits of reform. In one case in particular, this took the shape of providing a forum for an intensive two-day workshop in Washington to evaluate and discuss the administration's proposals with other member's of the Colombian government.

In the end, the country's adoption of the reform agenda and its success was due to their ownership of the program. The genesis of the program was entirely Colombian. The World Bank's primary contribution for the reforms came from providing some "behind-the-scenes" incentives to complete the program through lending and analytical support.

The total time from the date of the World Bank's initial identification mission to first disbursement was less than 11 months. This includes the negotiations over the terms of the loan and the final approval of the loan by the World Bank's Board of Directors. The entire US$400 million loan was disbursed over 14 months; the first tranche was released on December 26, 2001 and the last tranche on February 21, 2003.

7.2 Supervision:

Bank performance in supervision is assessed as *satisfactory*. The implementation period of the SFAL was relatively short and the program required periodic supervision. The second tranche release took place 7 months after the scheduled expected release in March 2002. The delay was perhaps inevitable given the overly optimistic release date in the original loan proposal as well as the inevitable delays resulting during an election year and the change in government that occurred on August 7, 2002. To a large degree the loan program anticipated the difficulties arising from the change in government and worked to prepare a collection of policy notes to speed and smooth the transition from the Pastrana to the Uribe administration.

In general, the short timeframe of the program made the loan conditionality somewhat problematic and necessitated that fiscal targets be based primarily on approved (not executed budgets) and preliminary (rather than final) budget data. While the conditions for loan were met at the time of the tranche releases, with hindsight we found that the actual executed budget was typically higher than the approved budget. Rather than indicating a problem with the supervision of the program, it suggests that targets or conditions in fast disbursing loans should be based more on actions than on planned fiscal outcomes.

7.3 Overall Bank performance:
Overall Bank performance is assessed as *satisfactory*.

Borrower
7.4 Preparation:
The Borrower's performance is assessed as *satisfactory*. Because the program for reform was essentially that of the Colombian government, it was well prepared for its implementation. As mentioned above, the implementation period for the SFAL was a time of political transition, which had implications for its preparation and sustainability. In preparing the loan, the outgoing Pastrana administration made efforts to consult with opposition groups in order to ensure its support and sustainability in the coming administration.

7.5 Government implementation performance:
The government's implementation performance is assessed as *satisfactory*. There was a strong commitment on the part of the Ministry of Finance and Public Credit to implement the reforms in the SFAL. Despite the difficulties working with opposition parties, vested interests in various sectors, and a tumultuous external environment, the Ministry was able to push forward on many fiscal fronts. While the fiscal reform process remains incomplete, the objective of the SFAL—to begin the process of fiscal reform—was largely successful thanks to commitment of the implementing agency.

7.6 Implementing Agency:
The performance of the implementing agency is rated as *satisfactory*.

7.7 Overall Borrower performance:
Overall borrower performance is rated as *satisfactory*.

8. Lessons Learned

1. Government commitment is a critical factor for success.

The SFAL was designed to support a fiscal reform agenda developed by the Colombian government. Ownership of the reforms was a critical element for the success of the program, ensuring the necessary coordination and long-term commitment to the process. This commitment was even more important given that project implementation spanned two government administrations. The risk that the reform agenda would be marginalized by the new administration was identified in the project document. However, the Uribe administration understood the importance of reform and maintained government commitment to the program.

2. Institutional reform is a long-term process.

While many of the reforms supported by the SFAL have not been completed during the period of the loan, they have advanced substantially. In the case of the ISS, the SFAL did not fully achieve its goal of developing a sustainable model for the institution. A longer loan period would have provided the on-going support necessary to achieve more progress in this area. Alternatively, subsequent programmatic loans such as the FIAL I and II could have continued to support reform in this area, but the issue has not been addressed in these subsequent loans.

3. Fiscal adjustment requires careful selection of quantitative indicators.

Certain elements of the program were based on quantitative fiscal targets. These targets suffered from two problems given the short-term nature of the loan. Firstly, tranche releases were based on mid-year expenditure figures. As in many countries, spending is back-loaded towards the end of the year, which means that low apparent expenditure at mid-year eventually disappears by year-end. This was the case during the SFAL for Colombia—actual expenditures during the second half of the year were much higher than during the first half of the year. Secondly, conditions in the program used initially budgeted figures rather than actual expenditures. As is often the case, actual expenditures vary considerably when compared with the original budget. Indeed, during the period of the SFAL program there were sizable upward adjustments to initially proposed budgets during the second half of year. Again, the result was a planned adjustment by the government that did not fully materialize. If actual fiscal adjustment is the goal, the loan should be phased-in over a longer period, allowing for the use of year-end expenditure data. With fast disbursing loans, quantitative budget targets are often of little use because actual budget data are typically unavailable or, if they are, are only preliminary and subject to potentially large revisions. In such circumstances, either other observable targets should be used or quantitative targets should not be used at all. A longer loan period under the programmatic approach is now a viable means to side-step this problem, but this form of lending was not available at the time of the SFAL.

9. Partner Comments

(a) Borrower/implementing agency:

Recent studies from the Departamento Nacional de Planeacion (DNP), the Dirección de Apoyo Fiscal (DAF), and the Central Bank of Colombia all highlight the satisfactory subnational fiscal results.* In general, these studies show improvement in the fiscal health of the subnational non-financial public sector as follows: 1) a shift in the fiscal deficit from 1.19 percent of GDP in 2000, to a fiscal surplus of 0.07 percent of GDP in 2002, 2) a real decrease of personnel expenditure of 416 billion pesos in 2002 compared to 2000 for the regional departments and 273 billion pesos decrease for the municipalities in real terms, 3) a reduction in the subnational debt stock as a percentage of GDP from 8.4 percent in 2000 to 8.0 percent in 2002.

These results were achieved due to both fiscal adjustment and restructuring implemented as part of the laws 358, 549, 550, and 617. A key lesson from this has been the change in the subnational government culture toward more autonomy and fiscal responsibility. It is hoped that Law 819 will further this process and continue to improve financial planning and accountability within a medium-term planning framework. It is also important to mention the consensus between the national government, the Congress, and the subnational governments on the need for solid finances to serve as the base for further decentralization. Future work remains to clearly identify pension liabilities and allocate funds for them, also institutional strengthening to improve financial management, both of these will give sustainability to the fiscal adjustment already achieved.

Moreover, it is important to note that reform of the subnational alcohol taxes harmonized the rates of the national VAT taxes and the regional departmental consumption taxes. This, in turn, reduced smuggling and increased tax collection at the subnational level. Further, the increase in the surcharge on gasoline allowed both departmental and municipal collections to improve. Between January and September 2003 collections grew 29 percent compared to the same period in 2002. Finally, under Law 788 subnational governments were granted an improved legal framework for increasing collections without changing the tax base or tax rates. However, this could not be implemented because the Constitutional High Court declared it unconstitutional.

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*Fiscal evaluation of 82 municipalities in 2002 (DAF), the Report on the Fiscal Performance of Departments and Municipalities in 2002 and 2000 (DNP), Boletin Semestral de Finanzas Territoriales, end-December 2002 (Banco de la Republica).

(b) Cofinanciers:
n.a.

(c) Other partners (NGOs/private sector):
n.a.

10. Additional Information

Annex 1. Key Performance Indicators/Log Frame Matrix

Intergovernmental Fiscal Relations

Board Presentation

- The constitutional amendment *(Acto Legislativo* No. 1, of July 30, 2001) reforming the transfer of resources from the central government to subnationals has become effective, limiting the rate of growth of fiscal transfers to subnational governments and the rate of growth of the central administration operational expenditures for 2002 and there-after.

  This condition was met. The Constitutional amendment was published on 22nd August 2001. It contained limits on the growth of fiscal transfers to subnational governments (limited to inflation plus 2% for 2002-2005 and 2.5 % from 2006-2008) and created a single consolidated system for transfers (Sistema General de Participaciones). It limited the rate of growth of central administration operational expenditures (to inflation plus 1.5% until 2008).

- The government has submitted to Congress a draft law reforming the tax system of territorial entities (*Estatuto de Ingresos Territoriales*) to increase subnational tax revenues by more than 20 percent in real terms in the first year of its application term compared to realized tax revenues in 1999.

  The condition was met. The draft law No. 086, 2001 was presented to Congress on 6th September 2001. The law had as its goal a reorganization of the existing subnational tax system and the implementation of further tax reform to increase subnational revenues.

- The government has issued a decree to regulate debt and borrowing of territorial entities that will contribute to halting unsustainable borrowing, limiting bailouts, and eliminating discretionality in the treatment of debt. Since July 1, 2001, the territorial entities have received no bailouts or guarantees of their debt in accordance with Law 617/00.

  The condition was met. The government issued the decrees 2540, November 27, 2001 and Decree 610, April 2002 governing debt and borrowing by territorial entities. The government also required capital-risk weighting for subnational borrowing. The government has continued enforcing Law 617, and since July 1, 2001 has not provided to territorial entities any bailouts or guarantees of their debt.

Second Tranche

- The government is implementing the Constitutional amendment *(Acto Legislativo* No. 1, of July 30, 2001) in accordance with its terms, limiting the rate of growth of (a) total transfers to subnational governments to last year inflation plus 2 percentage points; and (b) the central administration's operational expenditures to last year inflation plus 1.5 (percentage points)-as both were included in the FY02 budget, approved by Congress.

  This condition was met. The budget for 2002 and 2003 included limitations in the value of transfers and in the central administration operational expenditures in compliance with the Acto Legislativo No.1, 2001. The executed budget in 2002 complied with these restrictions.

- The decree governing debt and borrowing by territorial entities (referred to in condition 3 of the first tranche) is being implemented in accordance with its terms.

This condition was met. The government and the superintendence of Banks have satisfactorily enforced the decrees regulating subnational borrowing. In 2003 the government continued this process by approving Law 819 on fiscal responsibility which aimed to further tighten regulation, limiting central government involvement in bailouts and guarantees and establishing clear rules for debt management at sub-national level.

<u>Floating Tranche</u>

- Congress has approved the law referred to in condition 2 (first tranche), substantially in accordance with the proposal submitted by the government.

  This condition was mostly met. Although the draft Law 86 to which the tranche condition refers was not approved, in December 2002 Congress passed Law 788-2002 that contained substantial reforms to subnational taxes, in line with the reforms considered in the previous draft law. Principally the law considered (a) a rationalization of departmental and district taxes on distilled alcoholic drinks; (b) increases in the surcharges to gasoline charged by municipalities, districts and departments; (c) norms on the taxable value of mortgages and open collaterals and the use of public-private systems for collecting registry taxes; and (d) norms on tax procedures for departments and municipalities. Law 788-2002 did not include norms on territorial taxes that provided for all the tax increases and standardization of sources of income for territorial entities that had appeared originally in the draft law,however, the aim of increasing subnational revenue by more than 20% (a condition of the first tranche release) was met and reform in this area is still ongoing. In order to allow release of the floating tranche a waiver was secured by the Board in this case.

Health Reform

<u>Board Presentation</u>

- The Ministry of Health, the Department of National Planning, and the Ministry of Finance have defined and approved a national public hospital restructuring policy and an implementation program for the next five years, and have begun the implementation of the first phase, including the selection of at least 10 departments. For the year 2002, the implementation program has covered more than 15 percent of the total public hospital budget included in the FYOI budget.

  This condition was met. The National Hospital Restructuring Policy was defined and approved and an implementation program was presented. The pilot phase of the program for 2002 covered more than ten departments and 15% of the total hospital budget.

<u>Second Tranche</u>

- The government has signed contracts with at least three subnational governments to finance the restructuring of public hospitals, and the implementation thereof has started. These contracts have included specific annual targets for (a) productivity increases in inpatient and outpatient services and (b) labor cost reductions. The resulting fiscal savings are equivalent to at least 5 percent in real terms per month, on average among those participating subnational governments, compared to the previous year in a manner satisfactory to the Bank.

This condition was met. As of tranche release the government had signed contracts with six subnational governments for restructuring the hospital network, which included the required improvements in service and reductions in cost. The resulting financial savings also met the requirements of generating a minimum of 5% savings in real terms a month. By the end of 2002 the government was implementing the hospital-restructuring plan in 26 hospitals. For these hospitals, total spending had fallen by 18% comparing 2002 with 1999 whilst medical consultations were up 31% and surgeries were up 23%. The pilot project has been deemed to be highly successful and as financing becomes available, implementation will continue to be scaled up.

- The government has transformed 60 percent or more of the 2001 budgeted health *situado fiscal* (after legal mandatory deductions) to demand subsidies.

  The condition was met. At the time of tranche release the government had transformed 63% of the health "situado fiscal" from supply to demand subsidies.

ISS (Instituto de Seguro Social) Reform

Board Presentation

- The government has initiated a restructuring plan for ISS Health, including negotiating with ISS unions about labor costs and benefits, and has implemented the first phase, including the completion of renegotiating 50 percent or more of ISS's total outstanding debt to health service providers and the reduction in at least 30 percent in the waiting list for elective surgeries (as of June 30, 2001).

  This condition was met. An ISS restructuring plan was developed and approved by the board of the ISS; a new collective bargaining agreement was signed between the President of the ISS and representatives of the trade union; there was a reduction in the waiting list for pending surgeries as agreed; and a restructuring of ISS pending debt.

Second Tranche

- The government and the ISS have reached agreement to generate annual savings in ISS' total costs over a 10-year period, which will, in the opinion of the Bank, make ISS financially and economically viable.

  This condition was met. Further to the measures mentioned above, efforts were undertaken to improve ISS financial management, 8,000 vacant positions were removed, 20 ambulatory health facilities were closed, new regulations for health service co-payments were implemented and the ISS was generally downsized. These important reforms, whilst improving the possibility that the ISS may become financially and economically viable, have not resolved this issue definitely and the closing the ISS remains a serious option. Doubts remain about financial sustainablity ISS, despite continuing efforts to reform the institution.

Pension Reform

Board Presentation

- The government has created a new social security department in the Ministry of Finance for improving social security system control and sustainability. Improved control has generated fiscal savings equivalent to more than US$100 million in 2001.

This condition was met. The government established an agency in the Ministry of Finance (la Dirección de Regulación de Seguridad Social) to review policies, make regulatory recommendations, and oversee programs that generated savings estimated at US$300 million during 2001.

<u>Second Tranche</u>

- The government is carrying out and controlling the transfers of public pension regimes into a single agency, reducing payments of ineligible pension claims. Ongoing controls generate fiscal savings of, on average, at least US$10 million per month.

  This condition was met. The government was successfully carrying out and controlling the transfer of public pensions into a single agency, greatly reducing payments of ineligible pensions claims. Ongoing controls continue to generate substantial fiscal savings.In only the first quarter of 2002, control and recalculation of claims had yielded reductions in the present value of claims equivalent to US$ 80 million.

<u>Floating Tranche</u>

- Congress has approved a law to reform the general pension system to put it on a sustainable path; or Congress has approved a law to reform at east one of the exempted pension regimes to bring it/them, in the opinion of the Bank, in line with the general pension regime.

  The secondary condition was met, and the primary condition was largely met. Pension reform was passed in Congress in December 2002. The Law stipulates that all new workers of ECOPETROL will now join the general pension system instead of the separate system that was available to them before. The Law also made reforms providing for an increase in the rate of contribution, a reduction in the replacement ratio and a gradual increase in the contribution period. This has meant that new entrant into the system will not add to the actuarial deficit. The referendum scheduled for 2003 will also propose adding a ceiling of 25 minimum wages to pensions paid by the public sector and abolishing all special pension regimes in 2007.

Public Sector Reform

<u>Board Presentation</u>

- The government's approved budget for FY02 has included a reduction in total central government current expenditure (net of interest payments and transfers to subnational entities and to social security) of more than 4 percent in real terms in relation to the same expenditures in the approved budget for FY0I.

  This condition was met. The approved budget for FY2002 for current expenditure had been reduced by more than 4%, as compared with the FY2001 budget in force. However, the 2001 budget in force at the time of tranche release had already increased significantly. Comparing the 2002 initially approved budget with the 2001 initially approved budget would have shown an increase in FY2002 *of 4% in real terms.*

- The government's approved budget for FY02 has included a reduction in central government's general expenditures *(gastos generales)* of more than 15 percent in real terms in relation to the same expenditures in the FY00 executed budget.

  The condition was mostly met. The approved budget for FY2002 included a reduction in general expenditures of 12.5 % in real terms as compared with expenditures for the same items in FY2000.

<u>Second Tranche</u>

- The central government's total actual current expenditures (net of interest payments and transfers to subnational governments and to social security) that are being incurred in 2002 are generating average savings of more than 4 percent in real terms in relation to the same expenditures incurred during the same period in 2001.

  This condition was met at the time of the tranche. The evidence at time of tranche release based on figures for the first two quarters of FY2002 indicated spending on current expenditures had fallen by more than 4% in real terms as compared with spending as of second quarter FY2001. However, by year end, spending in this area actually represented an increase in real terms over spending in 2001 of 4%.

- The budget approved for FY02 has included general expenditures *(gastos generales)* that in real terms are not higher than those executed in the FY01 budget.

  This condition was met at the time of the tranche. The approved budget for FY2002 for general expenditures showed a decrease of 18.8% in real terms as compared with the FY2001 executed budget. However, going beyond the initial tranche release conditionality, it is interesting to note that by year end actual spending in FY2002 for general expenditures had increased by about 16% in real terms as compared with spending in the same period in 2001 and represented an increase of around 44% over the amount originally budgeted for FY2002.

Education

<u>Second Tranche</u>

- (a) Law 60, 1993 has been amended to provide for certification of municipalities that, together with districts, represent at least 40 percent of the country's school enrollment enabling such municipalities to autonomously manage the provision of education services (including teacher payroll) and to establish education performance monitoring mechanisms; or (b) the central government has certified municipalities that, together with districts, represent at least 14 percent of the country's school enrollment enabling such municipalities to autonomously manage the provision of education services (including teacher payroll) and intergovernmental performance agreements have been signed between the Central Government and such certified districts and municipalities. In either case, no extra budgetary transfers for education to certified districts or municipalities have taken place.

  This condition was met. Congress passed Law 715 of 2001, amending Law 60 of 1993 and *automatically certified for management of education services all municipalities that either (a) are capitals of departments, or (b) have more than 100,000 inhabitants. The automatic certifications represented more than 40% of the country's school enrollment for autonomous management, and have established education performance monitoring mechanisms. The national government singed inter-government performance agreements with 4 districts and 3 municipalities as of tranche release. At that time no extra budgetary resources had been transferred.*

Annex 2. Project Costs and Financing

Project Cost by Component (in US$ million equivalent)

Component	Appraisal Estimate US$ million	Actual/Latest Estimate US$ million	Percentage of Appraisal
Total Baseline Cost	0.00	0.00	
Total Project Costs	0.00		
Total Financing Required	0.00	0.00	

Project Costs by Procurement Arrangements (Appraisal Estimate) (US$ million equivalent)

Expenditure Category	Procurement Method[1]				Total Cost
	ICB	NCB	Other[2]	N.B.F.	
1. Works	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
2. Goods	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
3. Services	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
4. Miscellaneous	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
5. Miscellaneous	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
6. Miscellaneous	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
Total	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)

Project Costs by Procurement Arrangements (Actual/Latest Estimate) (US$ million equivalent)

Expenditure Category	Procurement Method[1]				Total Cost
	ICB	NCB	Other[2]	N.B.F.	
1. Works	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
2. Goods	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
3. Services	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
4. Miscellaneous	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
5. Miscellaneous	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
6. Miscellaneous	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)

Total	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)

[1/] Figures in parenthesis are the amounts to be financed by the Bank Loan. All costs include contingencies.

[2/] Includes civil works and goods to be procured through national shopping, consulting services, services of contracted staff of the project management office, training, technical assistance services, and incremental operating costs related to (i) managing the project, and (ii) re-lending project funds to local government units.

Project Financing by Component (in US$ million equivalent)

Component	Appraisal Estimate			Actual/Latest Estimate			Percentage of Appraisal		
	Bank	**Govt.**	**CoF.**	**Bank**	**Govt.**	**CoF.**	**Bank**	**Govt.**	**CoF.**

Annex 3. Economic Costs and Benefits

It was not possible to calculate the economic costs and benefits for this project.

Annex 4. Bank Inputs

(a) Missions:

Stage of Project Cycle	No. of Persons and Specialty (e.g. 2 Economists, 1 FMS, etc.)		Performance Rating	
Month/Year	Count	Specialty	Implementation Progress	Development Objective
Identification/Preparation				
21 Feb. to 2 March, 2001	*12*	TTL (2); Consultant (2); Program Asst. (1) Economists (Health, Pensions, Macro, Fiscal) (5) Decentralization (1)	S	S
3 to 5 April, 2001	*11*	TTL (2); Consultant (2); Program Asst. (1) Economists (Health, Pensions, Macro, Fiscal) (5) Decentralization (1) meeting with counterparts/officials in Washington, DC	S	S
21 to 25 May, 2001	*12*	TTL (2); Consultant (2); Program Asst. (1) Economists (Health, Pensions, Macro, Fiscal) (5) Decentralization (1) Legal (1)	S	S
18 to 21 July, 2001	*12*	TTL (2); Consultant (2); Program Asst. (1) Economists (Health, Pensions, Macro, Fiscal) (5) Decentralization (1) Legal (1)	S	S
Appraisal/Negotiation				
7 to 9 November, 2001	*12*	TTL (2); Consultant (2); Program Asst. (1) Economists (Health, Pensions, Macro, Fiscal) (5) Decentralization (1) Legal (1) negotiations took place in Bogota at the Bank's office.	S	S
Supervision				
14 to 19 January, 2002	*2*	TTL (2)	S	S
21 to 22 February, 2002	*2*	TTL (2)	S	S
30 August, 2002	*7*	TTL (2); Consultant (1); Health Sector/ISS (1); Social Security/ISS (1); Decntralization (1); Legal (1)	S	S
			S	S
ICR				
21 to 25 September, 2003	*1*	TTL(1)	S	S

(b) Staff:

Stage of Project Cycle	Actual/Latest Estimate	
	No. Staff weeks	US$ ('000)
Identification/Preparation		
Appraisal/Negotiation		
Supervision		
ICR		
Total		

Annex 5. Ratings for Achievement of Objectives/Outputs of Components

(H=High, SU=Substantial, M=Modest, N=Negligible, NA=Not Applicable)

	Rating
☒ *Macro policies*	○ H ○ SU ● M ○ N ○ NA
☒ *Sector Policies*	○ H ● SU ○ M ○ N ○ NA
☐ *Physical*	○ H ○ SU ○ M ○ N ● NA
☐ *Financial*	○ H ○ SU ○ M ○ N ● NA
☒ *Institutional Development*	○ H ● SU ○ M ○ N ○ NA
☐ *Environmental*	○ H ○ SU ○ M ○ N ● NA
Social	
☒ *Poverty Reduction*	○ H ○ SU ● M ○ N ○ NA
☐ *Gender*	○ H ○ SU ○ M ○ N ● NA
☐ *Other (Please specify)*	○ H ○ SU ○ M ○ N ● NA
☐ *Private sector development*	○ H ○ SU ○ M ○ N ● NA
☒ *Public sector management*	○ H ● SU ○ M ○ N ○ NA
☐ *Other (Please specify)*	○ H ○ SU ○ M ○ N ● NA

Annex 6. Ratings of Bank and Borrower Performance

(HS=Highly Satisfactory, S=Satisfactory, U=Unsatisfactory, HU=Highly Unsatisfactory)

6.1 Bank performance	*Rating*			
☒ *Lending*	○ *HS*	● *S*	○ *U*	○ *HU*
☒ *Supervision*	○ *HS*	● *S*	○ *U*	○ *HU*
☒ *Overall*	○ *HS*	● *S*	○ *U*	○ *HU*

6.2 Borrower performance	*Rating*			
☒ *Preparation*	○ *HS*	● *S*	○ *U*	○ *HU*
☒ *Government implementation performance*	○ *HS*	● *S*	○ *U*	○ *HU*
☒ *Implementation agency performance*	○ *HS*	● *S*	○ *U*	○ *HU*
☒ *Overall*	○ *HS*	● *S*	○ *U*	○ *HU*

Annex 7. List of Supporting Documents

Comments of borrowers in original Spanish

Comentarios del prestatario (DAF)

El logro de resultados fiscales satisfactorios en los gobiernos subnacionles se manifiesta en evaluaciones recientes hechas por la DAF (Viabilidad Fiscal departamental 2002, evaluación fiscal de 82 municipios 2002), el Departamento Nacional de Planeación (Informe sobre el desempeño fiscal de los departamentos y municipios año 2002 y comparativo 2000) y el Banco de la República (Boletín semestral de finanzas territoriales, cierre a diciembre de 2002). En general estos estudios muestran el saneamiento fiscal del Sector Público No Financiero Territorial en los siguientes términos: paso de una situación de déficit del orden de 1.19% del PIB en el 2000 a una de superávit de 0.07% del PIB en el 2002; disminución real, medidos en pesos de 2002, de los gastos de personal del año 2002 frente al 2000 por $416 mil millones de pesos en los departamentos y $273 mil millones en los municipios; disminución del saldo de la deuda territorial como porcentaje del PIB de 8.4% en el 2000 a 8% en el 2002. Estos resultados se alcanzaron gracias a la aplicación conjunta de medidas de ajuste y reestructuración fiscal puestas en marcha en el marco de las leyes 358, 549 y 550 y 617. Una de las lecciones más importantes de este proceso es el cambio de cultura impulsado por las reformas, hacia el ejercicio de una autonomía con responsabilidad fiscal por parte de los gobiernos departamentales y municipales, la cual se espera consolidar mediante la aplicación de la ley 819, en la cual se fijan procesos y procedimientos dirigidos a mejorar la planeación financiera, y la rendición de cuentas, mediante referentes claros de mediano plazo para la toma de decisiones en materia de ingresos, gastos y deuda. A nivel institucional, cabe destacar el logro de consensos básicos entre el gobierno nacional el Congreso y los gobiernos subnacionales alrededor del objetivo de profundizar la descentralización sobre bases financieras sólidas. Los principales aspectos en los cuales se debe trabajar a futuro son la depuración y provisión del pasivo pensional y el fortalecimiento institucional orientado a una mejor gestión financiera, aspectos endógenos que le darán sostenibilidad a los ajustes alcanzados.

De manera particular, la reformas a los tributos territoriales de licores permitieron homogenizar las tarifas de los impuestos nacionales (IVA) y los departamentales (consumo), lo cual racionalizó la carga tributaria a favor del consumo logrando disminuir el contrabando y aumentar el recaudo a favor de las entidades territoriales. Por otra parte, el aumento de la tarifa de la sobretasa a la gasolina permitió aumentar los recuados departamentales y municipales: para el período enero-septiembre de 2003 éstos crecieron 29% respecto al mismo período de 2002. Finalmente, con el fin de dotar a las entidades territoriales de mejores herramientas legales para aumentar sus recaudos sin cambiar bases gravables ni tarifas, el gobierno nacional, en el marco de las facultades otorgadas por la ley 788 elaboró un régimen procedimental y sancionatorio, que, sin embargo, no pudo ser convertido en en decreto con fuerza de ley, dado que la Corte Constitucional declaró inexequible las facultados previstas para tal fin en la ley 788.