

FISCAL STRENGTHENING SUPPORT TO CARIBBEAN COUNTRIES

RG-T2315

CERTIFICATION

I hereby certify that this operation was approved for financing under the **Special Program for Institutional Development (PID)** through a communication dated June 17, 2016 and signed by Kai Hertz (ORP/GCM). Also, I certify that resources from said fund are available for up to **US\$300,000** in order to finance the activities described and budgeted in this document. This certification reserves resource for the referenced project for a period of four (4) calendar months counted from the date of eligibility from the funding source. If the project is not approved by the IDB within that period, the reserve of resources will be cancelled, except in the case a new certification is granted. The commitment and disbursement of these resources shall be made only by the Bank in US dollars. The same currency shall be used to stipulate the remuneration and payments to consultants, except in the case of local consultants working in their own borrowing member country who shall have their remuneration defined and paid in the currency of such country. No resources of the Fund shall be made available to cover amounts greater than the amount certified herein above for the implementation of this operation. Amounts greater than the certified amount may arise from commitments on contracts denominated in a currency other than the Fund currency, resulting in currency exchange rate differences, represent a risk that will not be absorbed by the Fund.

Original firmado

Sonia M. Rivera
Chief

Grants and Co-Financing Management Unit
ORP/GCM

09/09/16

Date

Approved:

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IFD/FMM

09/20/2016

Date

TC Document

I. Basic Information

- Country/Region: Regional/CCB - Caribbean Group
- TC Name: Fiscal Strengthening Support to Caribbean Countries
- TC Number: RG-T2315
- Team Leader/Members: Gerardo Reyes-Tagle (IFD/FMM), Team Leader; Betina Hennig (LEG/SGO); Carola Pessino; Carlos Leon; Karl Edward Garbacik; and Maria Lorena Kevish (IFD/FMM).
- Taxonomy: Research & Dissemination
- Date of TC Abstract: 17 June 2016
- Beneficiary: Ministries of Finance in Jamaica, Suriname, Trinidad and Tobago; and the Caribbean Regional Technical Assistance Centre (CARTAC)
- Executing Agency: Inter-American Development Bank (IDB) through the Fiscal and Municipal Management Division (IFD/FMM)
- Donors providing funding: Special Program for Institutional Development (SPID)
- IDB Funding Requested: \$300,000
- Disbursement period: 30 months
- Required start date: October, 2016
- Types of consultants: Individuals consultants and firms
- Prepared by Unit: IFD/FMM
- Unit of Disbursement Responsibility: Institutions for Development Sector (IFD)
- TC Included in Country Strategy: No
- TC included in CPD (y/n): No
- GCI-9 Sector Priority: Institutions for growth and social welfare

II. OBJECTIVES AND JUSTIFICATION

- 2.1 The overall objective of this Technical Cooperation (TC) is to support the Caribbean Region efforts to achieve sustainable improvements in their fiscal management systems specifically related to tax administration and policy, budget policy, financial management, and public investment. For this purpose the TC will focus on creating a program for expanding institutional capacity and supporting policy reform to ensure fiscal sustainability in the Caribbean Region. This TC will include utilizing the Caribbean Regional Technical Assistance Centre (CARTAC)¹ to implement tax administration institutional strengthening programs in concert with the Bank's efforts to reform tax policy; improve budget planning; and address inefficiencies in the mechanisms for public investment.
- 2.2 Tax administration is weak within the Caribbean, resulting in low rates of compliance due to a lack of resources, outdated operational frameworks, and ineffective mandates to carry out audits and other enforcement measures across the entire tax spectrum rather than being efficiently targeted to maximize

¹ CARTAC has made tax administration a primary focus of its work for FY2017. Coordinating with CARTAC will provide efficiency benefits to this technical cooperation by ensuring there is no duplication of efforts, while also concentrating resources along a single work path.

compliance and revenue gains.² Programs to strengthen institutional capacity and update systems and frameworks are necessary and are being carried out by the countries in the region. For example, Jamaica has seen success with recently completed tax administration reform programs under the Bank-led programs that has reported increase in tax revenues (from 23.4% to 25% of GDP between 2013 and 2015) and is showing the desire to continue with new reforms. Suriname and Trinidad and Tobago stand to benefit from developing more efficient institutions that can maintain consistent revenue from a broad tax base, thereby being less reliant on natural resource exports for government revenues.³⁴

- 2.3 Implementing fiscal institutional strengthening and reform programs without also reforming tax policy is a lost opportunity. Jamaica's historical tax policy can be described as resting on a narrow tax base, inefficient and opaque operations, low compliance, and excessive use of distortionary and unproductive tax expenditures. Improving institutional capacity without reforming these would have produced little real effect, but the combination of both – as happened under the Bank's Fiscal Administration Modernization Program and the Fiscal Program for Economic Growth– contributed to a real increase in government revenues of 1% between 2014 and 2015. There are more tax policy reforms that should be conducted in Jamaica, and both Suriname and Trinidad and Tobago require technical assistance implementing tax policy reforms. The primary thrusts of these reforms will be consistent across all three countries: (i) reduce tax distortions (through broadening the tax base and reducing rates); (ii) reduce tax expenditures; and (iii) reduce informality.
- 2.4 Budget planning within many Caribbean countries is often a simple matter of creating a linear projection of revenue and expenditures and making adjustments to expenditures as the year continues. This is driven by a lack of resources as well as the lack of a better designed, but easily implementable framework for projections, and can create significant difficulties for government planning. For example, Suriname approved budget expenditures of 36% of GDP in 2015, but their actual expenditures amounted to only 29.7% of GDP. Despite this, their budget deficit was 8.8% of GDP. The complete disconnect between what was approved and the final outcome not only leaves little point in budgeting exercises in Suriname, but can be a major impediment to trust in the government as government commitments are not maintained. Administration and oversight of public investment projects is generally poor, resulting in low efficiency, when combined with high development and operational costs this can represent a severe drain on highly constrained public finances while providing little public benefit. Public investment cannot be expected to produce acceptable results-either fiscally or in terms of social welfare—under these conditions.

² See, for example, IDB/CARTAC 2005: Suriname Tax and Customs Administration Diagnostic.

³ In 2011, Suriname earned approximately 40% of government revenue from natural resource exports, equivalent to 10.7% of GDP. In 2015, it earned 15% of its revenue from natural resource exports, equivalent to 3.1% of GDP. Other factors did not make up for this decline in natural resource revenues, while expenditures also increased by almost 4% of GDP resulting in a deficit of 8.7% of GDP.

⁴ Trinidad and Tobago earned revenues equivalent to 17.6% of GDP from oil exports in 2011; these declined to an estimated 13% in 2015 and are projected to dip further to an average of 7% for the 2016-2021 time period. These revenue losses were partially mitigated by ongoing reforms, which brought non-energy revenues from 12.2% of GDP in 2011 to almost 19% of GDP in 2015, but further reforms will be needed to make up for the losses projected for the 2016-2021 time period. IMF 2016. Article IV Consultation.

III. DESCRIPTION OF ACTIVITIES, COMPONENTS AND BUDGET

- 3.1 **Component I: Tax Policy Reform.** Few countries in the Caribbean have successfully implemented a tax policy reform through broadening its tax base and removing many tax expenditures. Overall, in the Region, there is room to implement a number of tax reforms that can correct for the distortionary systems that prevail. Jamaica's success implementing a tax reform can stand as an example for Suriname and Trinidad and Tobago, both of which have a heavy reliance on narrow tax bases and a wide array of tax exemptions and tax expenditures. These countries are experiencing fiscal difficulties as a result of being exceedingly reliant on tax revenue from natural resource sectors with little revenue support from the available broader tax base of personal and corporate income taxes and sales taxes. This component includes: (i) diagnostics to identify weak or inefficient aspects of tax codes and tax policy; (ii) action plans to adjust or reform tax codes and tax policy to efficiently improve government revenue prospects; and (iii) implementation of pilot projects inspired by Jamaica's successful tax reform programs. A key focus of the tax reforms under this TC will be diagnostics to evaluate and calibrate the VAT in Trinidad and Tobago, and evaluate and design implementation of a VAT in Suriname especially with respect to the choice between a single rate or multiple VAT rates.
- 3.2 **Component II: Support Tax Administration Institutional Strengthening.** This component will support tax administration strengthening activities developed in coordination with CARTAC in accordance with Bank policies and procedures (but implemented by the Bank as the sole executor). These activities will take place in Jamaica, Suriname, and Trinidad and Tobago, with whom the Bank has ongoing programs. The activities under this component will complement the work that the Bank will be doing under components 1, 3 and 4. The primary stakeholder of this component will be the tax administration unit within each country's Ministry of Finance.
- 3.3 The tax administration institutional strengthening programs that will be implemented by the Bank in coordination with CARTAC fall under four areas of CARTAC's operational capacity: (i) diagnostics; (ii) preparation and implementation of plans; (iii) hands-on technical advice and training; and (iv) training programs for the dissemination of best practices. Joint efforts will center these reforms around: (i) diagnostic work to identify optimal electronic taxation and customs systems; (ii) development and implementation of plans to adopt advanced electronic taxation and customs systems, as well as revamp institutional structures to streamline them around the new, advanced electronic capacities; and (iii) ensure that tax and customs officials are well-trained and able to implement best practices in conjunction with their new electronic systems. Work with Jamaica will continue the efforts that have been underway for the past two years and will continue strengthening institutional capacity by further streamlining tax protocols within the Ministry of Finance and improving audit targeting to maximize compliance and revenue gain with a minimum of committed Ministry of Finance resources. Specific details of each of these components will be determined in consultation with CARTAC.
- 3.4 **Component III: Budget Planning Assistance.** There is little relation between approved government budgets and final government spending in the Caribbean,

which can obfuscate the usefulness of the budget as a policy tool and cast doubt on government commitments. Questions of whether programs or infrastructure will remain funded throughout the year can impede or delay private sector investment and activity while creating uncertainty for the general public, reducing the capacity of the market to operate in an efficient capacity. The Bank’s technical assistance will improve forecasting and budget frameworks to provide governments with a methodology that can be useful for policy implementation. In addition, more accurate budgeting methods will reduce market uncertainty, allowing the private sector and consumers to act with more confidence.

- 3.5 Implementing this component effectively will require not just improved technical methods but a new view of the budget as a commitment that should be kept if at all possible. This view of the budget, when coupled with improved technical methods, will renew the budget’s usefulness as a policy tool. This component includes: (i) diagnostics to identify efficiency gains in the budgeting process and methods for improved forecasting capacity; (ii) action plans to implement and train Ministry of Finance employees in new methodologies and processes; and (iii) implementation of pilot projects, such as training materials to implement streamlined budgeting methods. The primary stakeholder of this component will be the budget planning unit within each country’s Ministry of Finance.
- 3.6 **Component IV: Methods for Investment in Public Infrastructure.** Public investment in the Caribbean is generally poorly managed and often produces significant drains on government budgets, hindering economic growth at high monetary cost. Actions to improve public sector management, project evaluation, and procurement processes, as well as strengthening regulatory capacity of investment projects can produce large economic dividends in the medium- to long-run through improved infrastructure while reducing fiscal pressures. This component includes: (i) diagnostics to determine inefficiencies in the public investment process; (ii) action plans to correct inefficiencies in the public investment process; and (iii) pilot projects such as development and implementation of more efficient training programs and frameworks for project evaluation. The primary stakeholder of this component will be the public investment unit of each country’s respective Ministry of Finance.
- 3.7 **Component V: Knowledge and Dissemination of Results.** This component will finance the dissemination of lessons learned through implementation of the previous four components through the production of: (i) papers; (ii) blogs; and (iii) workshops, as coordinated with the SPID Technical Secretariat.

Table 1. Results Matrix

Indicator	Unit	Baseline	Baseline Year	EOP Target	Target Year	Means of Verification
Outcomes: Fiscal Systems, Tax Policy and Institutional Capacity Strengthening						
Reformed tax system	Tax code	0	2016	1	2018	Independent Consultant Report
Officials trained to utilize updated methodologies on tax administration	Individuals	0	2016	20	2018	Independent Consultant Report

Products						
Component I: Tax Policy Reform						
Plan for tax policy reform designed, including recommendations for value-added tax	Plan	0	2016	1	2018	Official report from the Ministry of Finance
Pilot Projects	Report	0	2016	1	2018	Independent Consultant Report
Component II: Support for CARTAC Tax Administration Institutional Strengthening						
Plan developed to implement new tax/customs systems and methodologies	Plan	0	2016	1	2018	Official report from the Ministry of Finance
Technical capacity building courses held	Courses	0	2016	4	2018	Independent Consultant Report
Component III: Budget Planning Assistance						
Develop plan to implement budget planning methodology improvements	Plan	0	2016	1	2018	Official report from the Ministry of Finance
Component IV: Methods for Investment in Public Infrastructure						
Develop plan to implement improvements to public investment procurement methods, including project evaluation and alternative procurement methods	Plan	0	2016	1	2018	Official report from the Ministry of Finance
Technical capacity building courses held	Courses	0	2016	2	2018	Independent Consultant Report
Develop plan to create a centralized information store of public infrastructure investment proposals, evaluations, and project information	Plan	0	2016	1	2018	Independent Consultant Report
Component V: Knowledge and Dissemination						
Publish papers on lessons learned from TC implementation	Study	0	2016	2	2018	Independent Consultant Report
Create blogs on lessons learned from TC implementation	Blogs	0	2016	4	2018	Independent Consultant Report
Hold workshops on lessons learned from TC implementation	Workshops	0	2016	2	2018	Independent Consultant Report

Table 2. Indicative Budget

Description	Bank Fund Funding	Counterpart Funding	Total
Component I	\$70,000	\$7,000	\$77,000
Component II	\$100,000	\$10,000	\$110,000
Component III	\$60,000	\$6,000	\$66,000
Component IV	\$60,000	\$6,000	\$66,000
Component V	\$10,000	\$1,000	\$11,000
Total	\$300,000	\$30,000	\$330,000

- 3.8 **Alignment with the Bank Strategies.** The Fiscal Strengthening Support to Caribbean Countries is aligned with the Updated Institutional Strategy (UIS) 2010-2020 (AB-3008); the Corporate Results Framework 2016-2019 (GN-2727-6) under the transversal result of institutional capacity and rule of law; the Fiscal Sector Framework (GN-2831-3); and the Sector Strategy Institutions for Growth and Welfare (GN-2587-2).

IV. EXECUTING AGENCY AND EXECUTION STRUCTURE

- 4.1 The Bank will execute the TC through the Fiscal and Municipal Management Division (FMM). It will ensure that the actions of this TC will synergize with current and future programs to create the most value for the member states with a minimum of operational redundancy.
- 4.2 The Bank will contract individual consultants, consulting firms and non-consulting services in accordance with the Bank's current procurement policies and procedures.

V. MAJOR ISSUES

- 5.1 The main risk of this TC is the potential for unforeseeable social, economic and climatological shocks that could stall or interrupt the proposed programs, delaying or stopping implementation. Strong government commitment will mitigate this risk, ensuring that programs are at most delayed.

VI. ENVIRONMENTAL AND SOCIAL STRATEGY

- 6.1 This TC has been classified as C based on the Safeguard Screening and Classification Toolkit. The results of this TC will contribute to the management of metropolitan governments and no adverse environmental or social impact is expected.

Required Annexes:

- Annex I: [Letter of Request](#)
- Annex II: [Terms of Reference for components](#)
- Annex III: [Procurement Plan](#)