

# Technical Cooperation Abstract

## I. Basic Project Data

- Country/Region: Regional
- TC Name: Modernization of Public Financial Management System at the Subnational Level
- TC Number: RG-T2635
- Team Leader/Members: Hyungon Kim, Team Leader; Axel Radics, Alternate Team Leader; and Carlos Pimenta (IFD/FMM); Emilio Pineda (FMM/CUR); Ramiro López Ghio (FMM/CCO); Belinda Perez (FMM/CDR); and Marina Massini (IFD/FMM).
- Taxonomy: Research and Dissemination
- Date of TC Abstract: August 2015
- Beneficiary: Latin America and the Caribbean countries
- Executing Agency: Inter-American Development Bank through Fiscal and Municipal Management Division (IFD/FMM)
- IDB Funding Requested: US\$600,000
- Execution period: 24 months; execution period: 30 months
- Required start date: October 2015
- Types of consultants: Firms and individual consultants
- Prepared by Unit: IFD/FMM
- Unit of Disbursement Responsibility: Institutions for Development Sector (IFD/IFD)
- Included in Country Strategy: No
- TC included in CPD: No
- GCI-9 Sector Priority: Institutions for growth and social welfare

## II. Objective and Justification

- 2.1 The objective of this Technical Cooperation (TC) is to identify challenges of Public Financial Management (PFM)<sup>1</sup> at the sub-national level in selected Latin America and the Caribbean (LAC) countries and recommend areas for improvement, with the end goal of making the handling of subnational public spending more transparent, effective and efficient.
- 2.2 PFM and Fiscal decentralization (FD) are two major pillars of public finance reforms, with potential to yield benefits to the overall public sector performance. These two reforms are expected to benefit each other. PFM reforms are vital for attaining the expected benefits of FD because of their critical role in maintaining fiscal discipline, efficient provision of public services, and accountability of sub-national government<sup>2</sup> (SNG) to higher levels of government and local constituents.
- 2.3 At the same time, the quality and performance of sub-national PFM are heavily dependent on the level and nature of FD; in other words, the spectrum of SNG varies considerably in their size, composition, and degree of autonomy among and within countries in LAC. Against this backdrop, the purpose of this TC is to contribute to explore current practices and systems in PFM at the sub-national level as well as to improve the effectiveness and openness of resource allocation and public service delivery.

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<sup>1</sup> PFM deals with the set of systems that cover all aspects of managing public resources, including resource mobilization and debt management. The key objectives of PFM is maintaining a sustainable fiscal position, the effective allocation of resources, and the efficient delivery of public goods and services (Cangiano, Curristine and Lazare, 2013).

<sup>2</sup> The term "sub-national government" includes all levels of government below the national level.

- 2.4 Through this TC, the framework to assess the current state of PFM at the sub-national level will be created and applied. In doing so, internationally standardized assessment tools such as Public Expenditure and Financial Accountability (PEFA)<sup>3</sup>, International Monetary Fund (IMF) Fiscal Transparency Code, and Open Budget Index may be benchmarked.
- 2.5 This project includes survey collection and data cleaning processes, the creation and sharing of regional and country data, individual country reports, and the promotion of regional policy dialogue. This is in line with GCI-9's strategic priority of strengthening institutions for growth and social welfare.

### **III. Description of activities and outputs**

- 3.1 **Component 1. Diagnosis of Current PFM and Establishment of Country Factsheets.** The basis of envisioning proper PFM reforms at the sub-national level is a fundamental understanding of a country's current system. For the accomplishment of this component, the framework to assess the state of subnational PFM will be created based on various standardized assessment tools such as PEFA, IMF Fiscal Transparency Code, and Open Budget Index. In addition, other indicators from the Public Expenditure Review (PER), the Country Financial Accountability Assessment (CFAA), IDB PRODEV's SEP may be referred to for the assessment.
- 3.2 A set of indicators coupled with diagnostic questionnaires also will be developed. And then, surveys for public servants at the national and subnational level in some countries will be conducted. Those countries will be selected based on different degrees and characteristics of FD.
  - a. Federal Country (e.g. Argentina): where FD reforms are fully in place. SNGs tend to have a relatively high degree of autonomy in collecting own revenue, borrowing power, and expenditure/revenue assignment.
  - b. Large Unitary Country (e.g. Colombia): where FD reforms at the intermediary stage. SNGs may have robust expenditure and revenue assignments but have limited discretion or autonomy in terms of taxing power, and expenditure decision.
  - c. Small Unitary Country (e.g. Dominican Republic): where the intermediate level of government does not exist or municipal government is the only instance of SNGs with a variety level of autonomy in taxation and expenditure decision.
- 3.3 **Component 2. Pilot Projects for the Creation of Policy Reform Platform.** Drawing on the findings from the survey, pilot projects in at least three selected countries will be conducted with the aim of creating a platform for PFM modernization at the sub-national level. For each country, a representative sample of SNGs will be selected according to criteria such as size, composition, and degree of autonomy and there will be thorough assessments through additional data collection and interviews with local officials. And then, the overall modernization plan of PFM at

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<sup>3</sup> For example, in the PEFA reports, each key indicator for PFM system is assessed in five input dimensions against what is perceived good international practice by PFM experts according to a 4-point calibration scale from A (highest) to D (lowest).

the sub-national level, along with a strategy to improve SNG capacity will be presented.

- 3.4 **Component 3. Knowledge Dissemination.** This component is to promote the regional policy dialogue through dissemination efforts including the publication of a book or paper. It will also provide a window for continuity of the cooperation framework on subnational PFM assessment and reform in the LAC region through dissemination events. In doing so, if possible, Korean experts will be identified to support this activity.

#### IV. Budget

- 4.1 The total cost of this operation has been estimated at US\$600,000, and will be financed by the Bank on a non-reimbursable basis.

**Table 1. Indicative Budget (US\$)**

Component	Description	IDB/Fund Funding	Total Funding
Component 1: Diagnosis of Current PFM and Establishment of Country Factsheets	Creation of the framework to assess the state of subnational PFM as well as surveys for public servants in some countries	360,000	
Component 2: Pilot Projects for the Creation of a Policy Reform Platform	In-depth Analysis on selected countries and individual consultant services and travel	168,000	
Component 3: Knowledge Dissemination	Publication of a book or paper and Dissemination events	52,000	
Miscellaneous		20,000	
<b>TOTAL</b>		<b>600,000</b>	<b>600,000</b>

#### V. Executing Agency and Execution Structure

- 5.1 The TC will be executed by the Bank, though Fiscal and Municipal Management Division (IFD/FMM) because this is a regional TC at subnational government level and the Bank is the better option in this case.

#### VI. Project Risks and Issues

- 6.1 The main risk would be that subnational governments might not be willing to participate in the data collection and validation process. To mitigate this risk, team members will leverage existing IDB networks such as the Latin American and Caribbean Community of Practice on Managing for Development Results (CoPLAC-GpRD) in order to foster regional ownership with this initiative.

#### VII. Environmental and Social Classification

- 7.1 There are no environmental or social risks associated with the activities outlined in this TC, therefore its environmental classification is [C](#).