

PROJECT INFORMATION DOCUMENT (PID) CONCEPT STAGE

Report No.: PIDC3164

Project Name	Social Protection System Modernization Project (P145171)
Region	EUROPE AND CENTRAL ASIA
Country	Croatia
Sector(s)	Other social services (100%)
Theme(s)	Social safety nets (100%)
Lending Instrument	Investment Project Financing
Project ID	P145171
Borrower(s)	Ministry of Finance
Implementing Agency	Ministry of Social Policy and Youth
Environmental Category	C-Not Required
Date PID Prepared/ Updated	10-Jan-2014
Date PID Approved/ Disclosed	17-Jan-2014
Estimated Date of Appraisal Completion	30-Jun-2014
Estimated Date of Board Approval	30-Sep-2014
Concept Review Decision	Track II - The review did authorize the preparation to continue

I. Introduction and Context

Country Context

Croatia has gone through five consecutive years of recession since the outbreak of the global financial crisis in 2008. By 2013, projected real GDP will be 12 percentage points lower than in 2008. The difficult external environment, slow progress in structural reforms and limited Foreign Direct Investment continue to limit growth prospects over medium term.

The prolonged crisis has led to a rise in poverty. Using an absolute poverty line fixed at 60 percent of median equivalent consumption in 2008, poverty increased by over three percentage points (from 13.3 percent in 2008 to a projected/ simulated 16.9 percent in 2012), disproportionately hitting middle-to-upper income households. The unemployment rate increased faster for men, reflecting the impact of the recession on sectors dominated by men, such as construction and manufacturing.

Spending on social welfare is high and was largely protected during the crisis. The share of spending on categorical benefits or entitlement is high, while the share of poverty- focused

programs is low. Administration of the many social assistance benefits is fragmented and inefficient.

Croatia joined the EU on 1 July, 2013. Since July 2013, Croatia is the 28 member of the European Union. Croatia now has access to significant EU grant financing.

Sectoral and Institutional Context

Croatia has a costly welfare system, about half of which is targeted at the poor and vulnerable. Almost half Croatia's non-contributory social assistance goes to war veterans and benefits - 1.8% GDP in 2011 and a further 1% is spent on a regressive child tax credit. However, the 2.4% GDP spent on cash transfer programs for the poor is well targeted and the poor are well covered by a combination of categorical and targeted social programs.

Cash benefit administration is fragmented across different ministries and agencies. While the Ministry of Social Policy and Youth (MSPY) has policy and budgetary authority for all pro-poor cash transfer programs, many are administered by other agencies, including child allowance, maternity benefits and birth allowances, unemployment benefits and some war veterans benefits (administered by the Pension Insurance Fund, the Health Insurance Fund, Public Employment Centers and Public Administration Offices respectively). Each of these agencies has its own office in each county across Croatia. This creates costs for beneficiaries applying for and receiving benefits, and augments the risk of error and fraud in the social assistance system.

Disability assessment (certification) is spread across five sectors/agencies with no harmonized methodology. Disability benefits in Croatia are among the highest in EU, next to Denmark, Sweden and Finland. With 3.6% GDP spent on disability programs (disability pensions, transfers, other benefits) in 2010, Croatia was 64% above EU 27. Such a high level is largely the legacy of the 1991-95 war, but also due to unstandardized and loose disability criteria, lack of control, and corruption in the disability assessment system scattered across pension, health, veteran, social, and education systems. Establishment of the Central Disability Certification Institute (CDCI) within the existing Fund for Professional Rehabilitation and Employment of Disabled Persons (FPREDP) in 2014 is expected to simplify the disability assessment process, harmonize the certification rules across different disability programs, reduce corruption and, in the long run, bring the costs of disability programs closer to the EU average.

It is likely that Croatia is losing significant amounts of money due to ineffective institutions and mechanisms to combat EF&C in the benefit system. Croatia operates a number of cash benefits with high a-priori risk of EFC, including income and means-tested programs (the child allowance and GMB programs), income replacement programs, disability pensions and allowances. The current delivery system of these benefits relies on preventive measures to stamp out EFC, but fall short of a comprehensive system. The capacity of the system to prevent or detect fraud is low. The only emphasis is put on prevention; detection efforts are minimal. The staff working on EFC activities is below 10 persons in each participating ministry or agency, substantially lower than in EU or other ECA countries. The investigative staff consists mainly of specialists in program certification rules (e.g. disability certification physicians or cash benefit administrators). Their expertise is not yet complemented by ICT and data analysts, which could make their work more efficient by narrowing the scope of the reviews or inspections to cases that are higher risk of EFC. The sanctions for error and fraud are also low or inexistent. Thus, the cost of defrauding the system is rather small (small probability of detection times weak recovery and sanction policy), while the benefits are positive

and, for some programs, very high.

The current features of social assistance programs could trigger work disincentives. The pool of working age individuals (between 15 and 64 years) who receive, directly or indirectly, social assistance transfers is large: 688 thousand persons out a total population of 4.2 million. Moreover, some social assistance programs are, in fact, income-replacement program offering generous benefits, such as the disability programs. Finally, some individual-level benefits are offered on condition that the beneficiary will not work, which has strong work disincentive effects. For these programs, introducing parametric changes that would strengthen work incentives and make work pay could be an effective measure to increase labor market participation of social assistance beneficiaries.

The legacy of State policies and practices in social care lingers in Croatia, with a continued reliance on residential care for vulnerable people. Croatia houses a high proportion of children without parental care and children and adults with development difficulties in institutions. Institutional care is necessary for those with severe disabilities, but many could live with foster families or in family-style units, which provide more humane environments and social inclusion for vulnerable populations. A de-institutionalization operational plan is being developed and should be ready by the end of 2013.

Relationship to CAS

The proposed operation would support two of the pillars in the Croatia Country Partnership Strategy FY14-17. Pillar 1 relates to Public Finance and within this Theme 1 aims to promote fiscal consolidation. The proposed project could deliver fiscal savings that would amount to 0.5-1 percent of GDP during the proposed project lifetime (2014-18). The proposed project would also support Pillar 3 of the CPS relating to maximizing the benefits of EU membership by helping the authorities to prepare for and access European Funds for activation and de-institutionalization.

The proposed project will build on existing operations and analytical work, including the Social Assistance chapter of the Public Finance Review and will complement other initiatives in the social protection domain, including; the ERDPL-2, which aims inter alia to increase the share of social protection programs that are means-tested; and a National Reform Program Technical Assistance, which is analyzing the options for a redesign of the Child Allowance and Child Tax Credit.

II. Proposed Development Objective(s)

Proposed Development Objective(s) (From PCN)

The proposed project will improve service delivery in social protection. It will aim to do this by: reducing fragmentation in the delivery of social assistance cash transfers; harmonizing disability certification procedures; reducing error and fraud in social assistance programs; supporting the adoption of incentives for work able social assistance beneficiaries to seek employment; and reducing the number of children and adults in residential institutions.

Key Results (From PCN)

1. Cumulative fiscal savings of at least 0.5% of GDP over the project lifetime;
2. Effective system to reduce error, fraud and corruption in risk-prone social protection programs in place;
3. Reduce private costs for social assistance beneficiaries and unemployed from x to y;
4. CDCI fully operational, including i) harmonized procedures to certify disability across all

disability benefits implemented, ii) full staffing, iii) regional network, iv) IT system with interfaces to OSS and other agencies;

5. Number of children without parental care and children and adults with disabilities moved from institutions to family-type living environments.

These individual results will contribute to the Government's longer term goals of promoting social inclusion for the poor and vulnerable, streamlining the social protection system and increasing labor force participation.

III. Preliminary Description

Concept Description

A. Concept

1. Description

The Government of Croatia (GoC) is undertaking an ambitious, wide-ranging reform agenda in social protection. The goal of the proposed reforms is to “achieve the financial and procedural rationality and efficiency of the social assistance system.” It aims to do this through consolidation of benefits using the support allowance program as a base for a new Guaranteed Minimum Benefit (GMB) program, which will provide the backbone of last-resort social assistance, by mid-2014; harmonization of the eligibility criteria for remaining benefits under MSPY's purview; improved information systems to promote better decision making and to reduce the scope for error and fraud. The proposed project aims at supporting the government's reforms of the social protection system, with a special focus on four areas: i) consolidation of programs and simplification of procedures; ii) reducing error fraud and corruption, iii) activation of social assistance beneficiaries; and iv) de-institutionalization.

Consolidation of programs and simplification of Procedures: One stop shop and Central Disability Certification Institute (CDCI)

A key element of the Government's reform is the consolidation of cash administration for social welfare programs, family policy programs and unemployment benefits through a single delivery network. Four social assistance benefits will be consolidated into a single GMB in the Ministry of Social Policy and Youth starting in January 2014. At the same time, a one-stop-shop (OSS) for administration and payment of cash benefits will be implemented. The OSS will gradually include a larger number of cash benefits, starting with the new GMB from September 2014, and later incorporating child allowances, maternity benefits, and unemployment benefits. The OSS, one of the highest priorities of the current government, will transform the experience of social assistance beneficiaries by providing a single service point to apply for and receive a range of cash benefits. Having a OSS will reduce the time and cost of application for beneficiaries and will create the opportunity of introducing a cap to the total amount of social assistance benefits paid to one household, generating potential for savings and reducing work disincentives associated with the provision of multiple need-based social assistance benefits.

Another major reform supported by the project is the creation of a Central Disability Certification Institute (CDCI). The reform, led by the MLSY and coordinated with the MLPS, will introduce a single certification procedure for persons with disability along the medical, social inclusion and work capacity domains. This reform will simplify administrative processes and harmonize

standards, and ensure horizontal equity for all persons with disability in Croatia. It is a revolutionary initiative, that it would encompass disability assessment procedures currently administered by several agencies including Croatian Pension Insurance Institute, Ministry of War Veterans, and Croatian Health Insurance Institute. Spending on disability benefits in Croatia is among the highest in EU, next to Denmark, Sweden and Finland. With 3.6% spent on disability programs in 2010, Croatia exceeded the eU27 average by 64%. Assuming that disability spending numbers would converge to 20% above the EU27 by 2035 (factoring in the objective disability factors in Croatia, such as Homeland war veterans' disability) could lead to cumulative fiscal saving between 10 and 11% of GDP over the next two decades, with savings of up to 1% over the project period.

Reducing Error, Fraud and Corruption

The Government is committed to tapping significant fiscal savings by developing the mechanisms and institutions needed to reduce the level of error and fraud in the social protection system. International evidence shows that any mass payment system is prone to error, fraud and corruption (EFC). In Croatia, benefits with high a-priori risk of EFC include income and means-tested programs (e.g., the child allowance and GMB programs), income-replacement programs, as well as disability pensions and allowances. The current delivery system of these benefits relies only on preventive measures to stamp out EFC, but fall short of a comprehensive system. Complementing these measures with an efficient detection and deterrence system will help safeguard the social protection system against EFC. The MSPY, MLP, Croatian Health Insurance Institute, Croatian Pension Insurance Institute and the Ministry of Public Administration agreed to work with the World Bank on identifying cutting edge EFC strategies and activities that could be applied to their benefits in the context of this project. It was also agreed that the project would support the application of EFC to the disability pension and allowances, where an important proportion of savings are expected to be generated. Support to the EFC agenda is expected to generate cumulative savings of 0.5-1% of GDP over the lifetime of the project.

Activation of Social Assistance Beneficiaries

The Government is keen in reforming social assistance programs and employment services to stimulate the labor market participation of social assistance beneficiaries. Croatia has a relatively large number of social assistance recipients that are able to work but do not work. About 35 percent of the beneficiary adults in the poorest quintile are not in employment, education, training, disabled or retired, and the share increases to 45 percent for beneficiaries of social assistance in cash. Partly, this is a reflection of the fact that poor households are often better off on assistance than on low-wage employment. Moving from assistance to employment would make them ineligible for means- and income-tested benefits, a feature of these programs that acts as an implicit tax on earnings. The Government could stimulate a higher employment rate by ensuring that the GMB and Child allowance programs reward work, and by offering tailored work support services to work-able beneficiaries from the poorest quintile. The project would support these efforts through specific technical assistance and by supporting the development of operational plans for using ESF for incentivizing and supporting the transition from assistance to employment for work-able adults from the poorest quintile. Activities would be defined during preparation and after an initial assessment of the working-age individuals who experience persistent labor market detachment, with a focus on those inactive who are beneficiaries of social assistance.

Deinstitutionalization

The MSPY's reform plans also encompass a process of deinstitutionalization in the provision of

social services currently implemented by State-run institutions. The goal of the proposed reforms is to shift the balance of service provision for key vulnerable groups from institutional, residential care to a range of services provided by a variety of service providers in family-type environments outside of the institutions. De-institutionalization can be a life-changing event for each individual, allowing independent, supported living through foster care, small housing units and other family-type environments. The Plan for Deinstitutionalization and Transformation of Social Welfare Homes (2011-18) will be translated into an Operational Plan by December 2013, describing the precise steps and sequencing of the deinstitutionalization process, including the number and rate of people to be deinstitutionalized (approximately 1,000 adults and children with mild disabilities and children without parental care). The project would support this reform; specifically, the Bank will assist the authorities with the design and focus of its proposals for European financing and reward the achievement of specific milestones. The funds disbursed from the project could then be channeled back into contributing to the Government's co-financing share for further European fund proposals.

The Project will take a results-based financing approach to the implementation of agreed activities under a first component of the project [E50m]. Thus, under this component, project disbursements would off-set Government expenditures on the new consolidated Guaranteed Minimum Benefit program (defined as the project's eligible expenditures); and would be triggered by the achievement of specific results ("Disbursement-Linked Indicators" or DLIs), agreed with the Government of Croatia, that track step increases towards key results, which will then trigger disbursements:

DLI 1: One Stop Shop. Possible DLIs (4): Disburse each time a Social Assistance program is transferred and being administered through the OSS: GMB, Maternity/Birth allowances, Child Allowances, Unemployment Benefits

DLI 2: Central Disability Certification Institute. Possible DLIs (4): Disburse with each development stage of CDCI: harmonized procedures implemented; full staffing across regional network; fully operational

DLI 3: Error Fraud and Corruption. Possible DLIs (4): Disburse when minimum EFC capacity is in place; Thematic inspections completed; Data cross checks with x other databases complete; Risk-based inspection completed

DLI 4: De-institutionalization. Possible DLIs (4): Disburse each time numerical milestones are met related to the number of children w/out parental care and children and adults with developmental difficulties transferred from institutions to family-type living environments

A detailed protocol would be prepared for each DLI, specifying the measures needed to meet it; who is responsible for gathering evidence of achievement etc.

Achievement of the DLIs would gradually lead to the achievement of the PDO over the project period. The main characteristics of the disbursement mechanism are: (a) each DLI would be associated with a specific value that would be disbursed upon achievement of the indicator; (b) the Government would provide evidence of achievement of each DLI, to be verified by the World Bank's technical team; (c) the World Bank will disburse the amount triggered by the DLIs that have been met. Disbursed funds would flow to the Croatian Treasury against expenditures made under the GMB program.

A second component [E20m] would support investments and technical assistance that are necessary, but not sufficient, to support achievement of the DLIs. Examples include: upgrades to the MIS to integrate systems currently used by other cash transfer programs and the IT system supporting

CDCI operations; technical assistance on cutting-edge error fraud and corruption techniques and investments in the prevention and detection infrastructure; training and technical assistance on disability certification methodology; and communications campaigns to raise public awareness of the reforms to social assistance and disability benefits and to attract foster families.

The Government has indicated it may request a Project Preparation Advance to support investments needed to make headway on project activities during the preparation period. Such activities could include the detailed needs assessment and preliminary drawings, analytical studies, and environmental assessments for renovations of one-stop-shops.

IV. Safeguard Policies that might apply

Safeguard Policies Triggered by the Project	Yes	No	TBD
Environmental Assessment OP/BP 4.01	x		
Natural Habitats OP/BP 4.04		x	
Forests OP/BP 4.36		x	
Pest Management OP 4.09		x	
Physical Cultural Resources OP/BP 4.11			x
Indigenous Peoples OP/BP 4.10		x	
Involuntary Resettlement OP/BP 4.12		x	
Safety of Dams OP/BP 4.37		x	
Projects on International Waterways OP/BP 7.50		x	
Projects in Disputed Areas OP/BP 7.60		x	

V. Financing (in USD Million)

Total Project Cost:	95.00	Total Bank Financing:	95.00
Financing Gap:	0.00		
Financing Source		Amount	
Borrower		0.00	
International Bank for Reconstruction and Development		95.00	
Total		95.00	

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