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R2014-0046/1

March 26, 2014

Closing Date: Monday, April 14, 2014 at 6 p.m.

FROM: Vice President and Corporate Secretary

Lebanon - Second Fiscal Management Reform Project

Project Appraisal Document

Attached is the Project Appraisal Document regarding a proposed loan to Lebanon for the Second Fiscal Management Reform Project (R2014-0046), which is being processed on an absence-of-objection basis.

Distribution:
- Executive Directors and Alternates
- President
- Bank Group Senior Management
- Vice Presidents, Bank, IFC and MIGA
- Directors and Department Heads, Bank, IFC and MIGA

Document of
The World Bank

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Report No: PAD549

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROJECT APPRAISAL DOCUMENT

ON A PROPOSED LOAN

IN THE AMOUNT OF US$5.2 MILLION

TO

THE LEBANESE REPUBLIC

FOR A

SECOND FISCAL MANAGEMENT REFORM PROJECT

March 19, 2014

Public Sector and Governance
Middle East and North Africa Region

CURRENCY EQUIVALENTS

Currency Unit	=	Lebanese Pound (LBP)
1,511 LBP	=	US$1

(Exchange Rate Effective March 13, 2014)

FISCAL YEAR
January 1 – December 31

ABBREVIATIONS AND ACRONYMS

BDL	Banque du Liban
CDR	Council of Development and Reconstruction
CPS	Country Partnership Strategy
CoA	Court of Accounts
CTB	Central Tender Bureau
CPS	World Bank Country Partnership Strategy
CQS	Selection Based on the Consultants' Qualifications
EdL	Electricite du Liban
EFMIS	Emergency Fiscal Management Reform Implementation Support Project
FMIS	Financial Management Integrated Information System
FBS	Selection under a Fixed Budget
FMR 2	Second Fiscal Management Reform Project
GMFIS	Government Fiscal Management Information System
GoL	Government of Lebanon
IFR	Interim unaudited Financial Reports
IoF	Institute of Finance
LCS	Least-Cost Selection
METAC	Middle East Regional Technical Assistance Center
MFD	Macro-Fiscal Department
MoF	Ministry of Finance
MTBF	Medium Term Budget Framework
MTDS	Medium Term Debt Strategy
MTEF	Medium Term Expenditure Framework
MTFF	Medium Term Fiscal Framework
POM	Project Operation Manual
PDD	Public Debt Directorate
PFM	Public Financial Management
PFS	Project Financial Statements
PMU	Project Management Unit
QCBS	Quality and Cost Based Selections
SBDs	Standard Bidding Documents Single
SSS	Single Source Selection
TOR	Terms of Reference
UNDP	United Nations Development Programme

Regional Vice President:	Inger Andersen
Country Director:	Ferid Belhaj
Acting Sector Director:	Bernard Funck
Sector Manager:	Guenter Heidenhof
Task Team Leader:	Joey Ghaleb

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ANNEXES

PAD DATA SHEET

Lebanon

Lebanon Fiscal Management Reform 2 (P133226)

PROJECT APPRAISAL DOCUMENT

MIDDLE EAST AND NORTH AFRICA
MNSPS

Report No.: PAD549

Basic Information			
Project ID P133226 Project Financing	Lending Instrument Investment	EA Category C - Not Required	Team Leader Joey Ghaleb
Project Implementation Start Date 14-Apr-2014 Expected Effectiveness Date 01-May-2014		Project Implementation End Date 30-Sep-2016 Expected Closing Date 31-March-2017	
Sector Manager Guenter Heidenhof	Acting Sector Director Bernard Funck	Country Director Ferid Belhaj	Regional Vice President Inger Andersen

Borrower: Ministry of Finance

Responsible Agency: Ministry of Finance

Contact:	Alain Bifani	Title:	Director General
Telephone:	961 1 642 722	Email: alainb@finance.gov.lb	

Project Financing Data(in USD Million)		
[X] Loan [ ] Credit	[ ] Grant [ ] Guarantee	[ ] Other

Total Project Cost:	5.20	Total Bank Financing:	5.20
Total Co-financing:		Financing Gap:	0.00

Financing Source	**Amount (US$M**
Borrower	0.00
International Bank for Reconstruction and Development	5.20
Total	5.20

Expected Disbursements (in USD Million)									
Bank Fiscal Year	2014	2015	2016	2017					
Annual	1.22	2.37	1.34	0.27					
Cumulative	1.22	3.59	4.93	5.20					

Proposed Development Objective(s)

The objectives of the Project are to strengthen the Recipient's capacity in fiscal policy analysis, debt management, and budgetary allocation of public resources; enhance the efficiency of the Recipient's financial management systems; and tighten the control environment for more effective use of the Recipient's public resources.

Components

Component Name	**Cost (USD Millions)**
1. Macro-Fiscal Analysis and Public Debt Management	
1.1 Macro-Fiscal Analysis	0.615
1.1 Public Debt Management	0.353
Subtotal	**0.968**
2. Public Expenditure Management,	
2. 1 Expenditure Programming and Budget Preparation	0.595
2.2 Budget Execution	1.996
2.3 Public Procurement Reforms	0.305
2.4 Internal Control and Internal Audit	0.352
Subtotal	**3.248**
Project Management Unit	**0.723**
Physical Contingencies	**0.261**
Total	**5.200**

Institutional Data

Sector Board

Economic Policy

Sectors / Climate Change

Sector (Maximum 5 and total % must equal 100)

Major Sector	Sector	%	Adaptation Co-benefits %	Mitigation Co-benefits %
Public Administration, Law, and Justice	Central government administration	100		
Total		100		

☑ I certify that there is no Adaptation and Mitigation Climate Change Co-benefits information applicable to this

Themes

Theme (Maximum 5 and total % must equal 100)

Major theme	Theme	%
Economic management	Debt management and fiscal sustainability	25
Economic management	Macroeconomic management	25
Public sector governance	Public expenditure, financial management and procurement	25
Public sector governance	Other public sector governance	25
Total		100

Compliance		
Policy		
Does the project depart from the CAS in content or in other significant respects?	Yes [ ]	No [X]
Does the project require any waivers of Bank policies?	Yes [ ]	No [X]
Have these been approved by Bank management?	Yes [ ]	No [ ]
Is approval for any policy waiver sought from the Board?	Yes [ ]	No [X]
Does the project meet the Regional criteria for readiness for implementation?	Yes [X]	No [ ]

Safeguard Policies Triggered by the Project	Yes	No
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

Legal Covenants

The Borrower shall through MOF establish, no later than one month after the Effective Date and thereafter maintain a PMU throughout the life of the project, with functions, staffing, resources and TOR satisfactory to the Bank, to be responsible for day-to-day project implementation

Name	Recurrent	Due Date	Frequency
		1 month after Effective Date	Once

Description of Covenant: The Borrower shall through MOF establish, no later than one month after the Effective Date and thereafter maintain a PMU throughout the life of the project, with functions, staffing, resources and TOR satisfactory to the Bank, to be responsible for day-to-day project implementation.

Conditions

Name	Type

Description of Condition

Team Composition

Bank Staff

Name	Title	Specialization	Unit
David A. Bontempo	Operations Analyst	Operations Analyst	MNSPS
Nada Abou-Rizk	Program Assistant	Program Assistant	MNCLB
Lars Jessen	Lead Financial Officer/Sovereign Debt	Lead Financial Officer/Sovereign Debt	FABDM
Lina Fares	Senior Procurement Specialist	Senior Procurement Specialist	MNAPC
Mona El-Chami	Sr Financial Management Specialist	Sr Financial Management Specialist	MNAFM
Wael Mansour	Country Economist	Team Member	MNSED
Joey Raymond Ghaleb	Sr Public Sector Spec.	Team Leader	MNSPS
Rock Jabbour	Financial Management Analyst	Financial Management Analyst	MNAFM
Rima Abdul-Amir Koteiche	Sr Financial Management Specialist	Sr Financial Management Specialist	MNAFM
Gretchen Melissa Biery	Senior Governance Specialist	Senior Governance Specialist	SASGP
Hassine Hedda	Finance Officer	Loan Operations	CTRLA

Non Bank Staff

Name	Title	Office Phone	City
William Hebb	IT Consultant	770-485-0878	Woodstock, GA

I. STRATEGIC CONTEXT

COUNTRY CONTEXT

1. ***Lebanon is an upper middle income country of 4.2 million people with a large diaspora and an average GDP per capita of around US$10,020 (in 2012).*** The country is highly urbanized with more than 85 percent of the population living in cities, and about half in the capital, Beirut. Lebanon has a services-oriented economy that accounts for 79 percent of GDP, followed by industry at 15.9 percent and agriculture at 5.1 percent.[1] The country has long been known not only for its political instability but also for its talented human capital, vibrant private sector, and open economy.

2. ***In contrast, the country's complex confessional-based political economy has deeply affected the quality of its public institutions.*** With poor services delivery and policy making, the public sector has not always been able to cope with the increasing requirements of the dynamic society and private sector. As a result, costly alternatives have been developed to cater for these needs. This has contributed to further deterioration in the competitiveness of the economy and the welfare of the population. Management of public finances is also weak. Budget laws have not been approved since 2006; public accounts have not been properly closed since 1993; and despite the Ministry of Finance's (MoF) considerable and continuing efforts to tackle significant gaps, weaknesses and lack of transparency remain present in the budgetary processes and practices.

3. ***Lebanon's large public debt, which recorded 134 percent of GDP in 2012, is a key binding economic constraint to future growth and social progress.*** It needs to be contained and reversed by structural fiscal adjustment especially with interest payments on debt averaging 9.8 percent of GDP in 2008-2012. This constituted around 32.1 percent of total public spending. In addition, the size and structure of the debt means that the exposure of the budget to changes in interest rates and exchange rates is very substantial. Lebanon has consistently run large budget deficits, averaging around 7.7 percent of GDP in the last five years. These large deficits have taken their toll on the macro stability of the country and its growth performance. The lack of fiscal space and the inefficient use of public resources have been an impediment to enhancing productive public investment, especially in infrastructure. The low capital expenditures, averaging 1.8 percent of GDP, has contributed to the deterioration in public service deliveries especially in sectors such as electricity, water and health. All have weakened social outcomes as Lebanese resort to expensive alternatives or receive poor services. Electricity outages and the transfers made to the electricity utility "Electricite du Liban" (EdL) that exceed five percent of GDP remain the most visible sign of such deterioration.

4. ***Lebanon is characterized by a large current account deficit (16.1 percent of GDP[2]) driven primarily by a structurally wide trade in goods deficit (31.8 percent of GDP[3]).*** To cover it, Lebanon attracts substantial inflows mainly in the form of short-term deposits and remittances. These come primarily from the large Lebanese diaspora and are pushed by increasing regional oil wealth, the attractiveness of the country's real estate assets, the resilience of the banking sector, and the lucrative interest rate spreads. These inflows have boosted aggregate demand and have

[1] The source of GDP and macro-economic data is the World Bank's Lebanon Economic Monitor Spring 2013.
[2] Average for the period 2008-2012.
[3] Average for the period 2008-2012.

strongly influenced economic policy. They also have contributed to relaxing the budget constraints of the country as a whole and may have delayed much needed fiscal adjustment.[4] As a result, the Central Bank (BDL) follows a policy of tightened regulations, costly sterilization, and foreign currency reserves build-up (currently exceeding 18 months of imports) so as to avoid asset bubbles and further deterioration in the real exchange rate and consequently the competitiveness of the economy. In this context, the role of fiscal policy is accentuated. Loose fiscal and budgetary disciplines in Lebanon continue to increase the pressure on the country's foreign exchange position and its pegged exchange rate regime.[5]

5. ***The fiscal challenges and the deterioration in public service delivery highlight the need for comprehensive and structural reforms.*** Lebanon faces several longstanding structural weaknesses, both at a micro- and macro-economic level. These concern (i) the equity of the tax system and its distributional function among factors of production, (ii) the need for civil service reforms, the role of the public sector and the quality of public service delivery, (iii) the scope of the social safety net program, including universal health coverage and pension reforms, (iv) the role of private sector development as a source of growth and employment creation, (v) the need for infrastructure investments in electricity, water and transport to alleviate as bottlenecks to growth and services delivery, and (vi) the cost of military armament program needed to maintain security stability in a context of political tensions and Syrian crisis ramifications. Improved fiscal policy and structural fiscal reforms are critical for implementing the above changes.

SECTORAL AND INSTITUTIONAL CONTEXT

6. ***The public financial management (PFM) system in Lebanon suffers from several constraints that hinder its proper functioning, weaken its transparency and make room for an inefficient use of public resources.*** Major impediments include: (i) an outdated and entangled PFM legislative and regulatory framework that imposes considerable inefficiencies within the budget cycle; (ii) a weak control environment that does not enforce the implementation of rules and guidelines; (iii) deficiency in human resource capacity and training, coupled with severe vacancies and skill mismatches in many areas of the PFM system; and (iv) a fragmentation in the budget and treasury functions. The above key challenges facing PFM in Lebanon are having negative effects on fiscal policy, governance and public service delivery.

7. ***The budget in Lebanon is largely integrated. The Central Government budget in Lebanon is structured into four components: a chapter for current spending, two chapters for capital spending that include references to multi-year investment programs[6], and an annex that includes the budget of revenue-generating entities.***[7] The central budget is integrated to a large extent with MoF taking the lead in preparing all components following one legislated process and using a unified GFS classification. Difficulties arise in managing multi-year investment programs, which have accumulated over the past decade and been voted into laws, as they cannot be revoked especially when earmarked projects are not executed.

[4] A thorough discussion on these issues can be found in the World Bank report "Using Lebanon's Large Capital Inflows to Foster Sustainable Long-Term Growth", World Bank Report No. 65994-LB, January 2012.
[5] Lebanon has been adopting a fixed exchange rate of the Lebanese Pound to the US Dollar since 2000.
[6] Called "lois programme". The multi-year programs are voted by the parliament and force the executive to allocate the required funds for the related projects.
[7] There are three entities : the telecommunication ministry, the national lottery, and the office of grains and beetroot.

8. ***Nevertheless, the budget falls short in terms of comprehensiveness.*** While all line ministries are accounted for in the budget law, many agencies and state-owned enterprises remain outside its scope. The latter are approved separately often by cabinet or in some instances by its governing board with no recurrence to parliament. This becomes problematic when such spending has implications on the central government budget, consequently introducing constraints to efficient cash planning and raising contingent liabilities risks. One notable case is the off-budget infrastructure spending of the Council of Development and Reconstruction (CDR).[8]

9. ***Lebanon has engaged on PFM reforms since 2007.*** As part of the Paris III donor conference for reconstruction in the aftermath of the 2006 Israeli hostilities, the Lebanese Government presented a comprehensive four-year reform program (2008-2011) in which it committed to reduce fiscal imbalances and stimulate growth. This came as one of the five pillars of the program calling for a phased fiscal adjustment with the objective of increasing primary surplus and reducing debt through streamlining expenditures and raising revenues measures. This triggered EFMIS[9] in 2008,[10] a broad based World Bank PFM support and capacity building project within MoF aimed at improving the control, allocation and use of public financial resources. The EFMIS project engaged on inter-linked measures in budgeting processes and practices both at the preparation and execution levels, and in debt and aid management.[11]

10. ***The deadlock over the budget since 2006 has stalled the PFM reform momentum.*** The political deadlock brought the executive and legislative branches in several instances to a standstill, forcing the Parliament not to adopt the successive draft budget laws since 2006. This situation created poor PFM practices and has set negative precedents. These were detrimental to the budget cycle processes as they weakened fiscal transparency, accountability and discipline. One example is the recurrence to treasury advances to overcome the financing constraints imposed by a lack of budget and the prevalence of the 1/12 rule of spending.[12] The continuous use of these instruments imposed considerable constraints in terms of accounting and controls. It also reduced transparency and increased inefficiencies in the use of public resources.

11. ***The commitment for PFM reforms was renewed in 2011. Fiscal reforms have been set as a priority area in the GoL's new economic program.***[13] This was visible through the accelerated pace observed in the activities of the EFMIS project in 2011-2013. During this period, MoF embarked on many notable structural reforms. These included (i) the review and closing of the public sector accounts since 1993, (ii) amendments to the outdated 1963 Public Accounting Law, (iii) the adoption of the new GFS 2001 classification, (iv) the creation of a cash management function with additional consolidation of public bank accounts, (v) the issuance of organizational

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[8] CDR is a government unit linked to the Prime Minister's office and is mandated in executing infrastructure projects on behalf of the Government. Its foreign financed infrastructure spending, through bilateral and multilateral sources, remains off-budget.

[9] Emergency Fiscal Management Reform Implementation Support Project (P111602).

[10] The project was prepared in 2008 and became effective in March 2009.

[11] For details on the objectives, activities and results framework of the EFMIS project please refer to the Project Document: *Emergency Fiscal Management Reform Implementation Support Project, Report No. 47456-LB, The World Bank, Washington DC, March 24 2009*.

[12] According to the Lebanese Public Accounting Law, the 1/12 rule of spending applies in the absence of a voted budget. In this case the government is authorized to spend on a monthly basis in accordance with the similar month of the last voted budget.

[13] Presented to Parliament during the vote of confidence.

decrees for launching and staffing the Public Debt Directorate, and (vi) technical improvements to secure the existing IT systems. The MoF also prepared strategies and action plans for further reform implementation. These include the comprehensive PFM reform strategy (2013-2017), the Budget Execution reforms action plan, and the FMIS[14] implementation strategy. These plans constitute the basis for the improvement of core PFM functions within the upcoming five years.

12. ***The PFM reform strategy articulates reform priorities, sets a direction and accelerates the work on relevant reforms.*** The guiding objective is to ensure efficient, effective and accountable use of public resources as a basis for economic development through improved public service delivery. The comprehensive strategy, entitled "strengthening the basics", focuses on five pillars: (i) Macro-fiscal analysis and forecasting, (ii) planning and budget preparation, (iii) budget execution, reporting and control, (iv) debt management, and (v) capacity building. The strategy identifies a list of tangible reforms to be implemented under each of the pillars within the time-frame 2013-2017. The strategy takes into account the need to tackle the basic business processes first and to strengthen simultaneously the MoF and line agencies.

13. ***The PFM reform agenda in Lebanon is being supported by several Donors.*** The UNDP has a long standing capacity building program within MoF in the areas of macro-fiscal analysis, debt management, and tax revenues. Parts of the tasks performed by this program are expected to be transferred to MoF in 2014. The IMF-METAC[15] provides short-term on- demand topical technical assistance (TA) services in various PFM reforms aspects. The EU on the other hand has launched a comprehensive twinning program in June 2013 tackling the organizational structure of the ministry and various aspects of the budget cycles. This twinning is also accompanied by a complementary TA project over the period 2013-2017. These reform activities are being coordinated with the World Bank so as to avoid potential overlap and exploit synergies within the supported projects and reform efforts.

14. ***The World Bank has been at the core of these PFM reforms working closely with MoF through the EFMIS project.*** The EFMIS project financed advisory services, training, and capacity building activities for implementing PFM reforms. The overall objective was to improve the control, allocation and use of public financial resources. This was implemented through a number of inter-linked activities in budgeting, debt and aid management designed to improve efficiency and transparency in government financial management. Many achievements have been made as a result of this technical assistance project including in:

i. *The institutional set-up:* the creation of public debt directorate and the macro-fiscal and cash management departments within MoF.
ii. *Strategic planning:* the formulation of a medium term fiscal framework, medium term debt management strategy, PFM reform strategy, and budget execution strategy.
iii. *Legislative and regulatory framework:* the preparation of a new draft budget systems law, and associated executive regulations, to replace the outdated 1963 public accounting law.
iv. *Business processes:* the introduction of new practices in accounting, reporting, commitment controls, cash management and forecasting, streamlining public accounts and cash collections, IT systems, budget classification (the introduction of GFS 2001), expenditure programming and budget preparation guidelines.

[14] Financial Management Integrated Information System.
[15] Middle East Regional Technical Assistance Center.

v. *Documentation:* documenting missing budgetary processes such as in accounting, commitment controls and others.

vi. *Capacity building and development of curricula*: several curricula were developed covering budget preparation, budget execution, debt management and others and training was delivered to staff in both MoF and other administrations.

15. ***The Second Fiscal Management Reform (FMR 2) project builds on the accelerated momentum for reforms under EFMIS and supports reform activities identified under the PFM strategy (2013-2017).*** The new project enhances and further deepens the reform activities initiated under EFMIS.

HIGHER LEVEL OBJECTIVES TO WHICH THE PROJECT CONTRIBUTES

16. ***Fiscal consolidation and improved allocation of public resources has been on the agenda of successive Lebanese governments.*** High levels of debt, large fiscal deficits, and lack of fiscal space for public investments have been identified as major constraints to the country's economic growth. Successive governments have all introduced fiscal reforms as a top priority in their economic programs for which they obtained the Parliament's vote of confidence. Despite tangible efforts made, fiscal outcomes have not consistently been favorable. With support from the EFMIS project, the MoF engaged on a comprehensive fiscal management reform agenda in the past four years. As a result, a PFM reform strategy for the medium term has been drafted. To oversee its implementation, the MoF recently created a PFM reforms steering committee that includes senior representatives from all Ministry functions. The FMR 2 project builds on the deliverables of EFMIS and is designed to work with the PFM reforms steering committee on implementing part of these reforms.

17. ***Capacity building and implementation support for public finance management and fiscal consolidation is a key element under the Lebanon Country Partnership Strategy (FY11-FY14)***[16] ***and is aligned with MENA's Regional Framework for Engagement, supporting the pillar on Governance.*** Fiscal management, governance and stability have been identified as the CPS's first area of engagement under the Tier I core program. The objective behind this engagement has been set to "achieve enough fiscal adjustment to generate sizeable primary surplus that has beneficial impact on efficiency and growth". The attainment of this objective hinges on a steady improvement in fiscal management and governance and a prudent management of public debt. Through working jointly with MoF and relevant government stakeholders on strengthening fiscal policy analysis capacity and reforming the budget cycle process and practices, the FMR 2 project is fully consistent with the objectives laid out by the CPS. The project is also complementary to other instruments of assistance, planned and underway, notably in the energy and the social protection sectors where the objective is to reduce fiscal costs, decrease reliance on subsidies, and improve on governance and services.

[16] Report 54690-LB discussed by the Board of Executive Directors in July 2010.

II. PROJECT DEVELOPMENT OBJECTIVES

PDO

18. ***The objectives of the Project are to strengthen the Recipient's capacity in fiscal policy analysis, debt management, and budgetary allocation of public resources; enhance the efficiency of the Recipient's financial management systems; and tighten the control environment for more effective use of the Recipient's public resources.***

PROJECT BENEFICIARIES

19. ***The FMR 2 project beneficiaries consist of the following two categories:***

a. *Ministry of Finance- Directorate General of Finance:* The project provides: (i) capacity building for staff from the different departments at the Ministry of Finance; and (ii) technical assistance for streamlining and aligning budget procedures and practices to international standards. Issues to be tackled cover macro-fiscal analysis, debt management, expenditure programming and budget preparation functions, along with budget execution procedures including accounting and reporting standards, cash management, internal audit and controls, procurement, and IT stabilization and FMIS design. The PFM reforms steering committee within the Ministry will serve as the project's technical counterpart while the Minister and Director General will play a strategic guidance role to oversee the implementation of the proposed reform measures.

b. *Other Government Institutions:* The project engages directly with several government entities on relevant budget reforms areas. The engagement varies by task and function performed by each entity in public financial management. This engagement therefore takes several forms, notabl capacity building including at least 50% women, technical assistance, consultations, or any combination thereof, and is addressed to the staff of the relevant institutions. The project identifies these entities as: (i) the Central Bank (BDL) where the engagement will focus on both debt and cash management; (ii) the Courts of Accounts (CA) on the control environment; (iii) selected line ministries where changes will be introduced to budget preparation, commitment controls and liquidation procedures; (iv) the Central Tender Board (CTB) on procurement related reforms, with the CTB benefitting from direct assistance through a defined sub-component within the project; and (v) the Institute of Finance (IoF) on training implementation aspects.

PDO LEVEL RESULTS INDICATORS

20. ***The progress toward the PDO will be monitored through the following key indicators (see Annex 1 for details on results indicators):***

a. Budget Framework Paper developed and submitted for cabinet discussion prior to issuance of the budget circular.
b. Domestic borrowing plans are formulated and published on an annual basis by the Public Debt Directorate (PDD).

c. Line ministries with detailed budgets prepared on time and as per the Medium Term Fiscal Framework guidelines.
d. The Ministry of Finance financial statements issued in compliance with IPSAS cash standards.
e. Annual internal audit report issued by the Ministry of Finance and approved by the relevant authority as defined by decree.
f. Number of trained staff, of which 50% are female.

III. PROJECT DESCRIPTION

PROJECT COMPONENTS

21. ***The proposed operation builds on the reform areas initiated by the EFMIS project, consolidates the outcomes already achieved under this project, and deepens the reform process with more focused, specialized and institutionalized activities.*** Moreover, the Ministry – with support from EFMIS - has developed strategies and action plans for further reforms in the PFM areas. These include a comprehensive PFM reform strategy (2013-2017), a budget execution reforms implementation plan, the FMIS implementation strategy and a comprehensive IT system audit. These plans constitute the basis for the improvement in core PFM functions within the upcoming five years. The proposed FMR 2 project is expected to support most of the key reform and change management activities.

22. ***The activities of FMR 2 are geared primarily towards building the capacity of the administration.*** FMR 2 activities focus on capacity building for civil servants and provide technical assistance to support the review and implementation of processes, procedures and practices related to the budget cycle. As such, the project is not contingent on policy decisions and is less exposed to the complex political context of Lebanon. The project empowers staff to provide more sound technical input for decision makers and hence adopts a bottom-up approach in that sense to improve policy making. Once politically conducive settings with no gridlocks at the legislative and the executive levels are present, the tools and capacity to perform further structural reforms in the PFM area will be ready.

23. ***FMR 2 comprises two broad complementary components.*** First, a Macro-fiscal Analysis and Public Debt Management component that focuses on building the policy functions at MoF. This component is divided into a macro-fiscal analysis and a debt management sub- component. Second, a Public Expenditure Management component that focuses on reforms of various practices and processes within the budget cycle. This component is divided into four sub- components: (i) expenditure programming and budget preparation reforms, (ii) budget execution, (iii) procurement reforms, and (iv) internal control and internal audit. A summary on the objectives and outcomes of these sub-components can be found below. Further background information and details on the activities supported by each sub-component are in Annex 2.

Component 1: Macro-Fiscal Analysis and Public Debt Management (US$0.968 million)

Sub-component 1.1: Macro-Fiscal Analysis (US$0.615 million)

24. ***Macro-fiscal analysis was absent from the core functions of MoF prior to the creation of the Macro-Fiscal Department (MFD) in March 2012.*** With support from EFMIS, the MFD

produced a Medium Term Fiscal Framework (MTFF) that was incorporated in the 2014 budget circular, using a macro-fiscal model developed in-house. Going forward, FMR 2 intends to support MoF in expanding the scope and the depth of operations to transform the MFD into a policy analysis unit within the Ministry. This requires long-term systemic capacity building.[17] The aim is to enable MFD to acquire the required skills to deliver the needed policy analyses and reports (e.g., impact analysis of fiscal measures on macroeconomic indicators) and ultimately become a self-reliant unit.

25. ***To achieve the stated objectives, a number of activities are envisioned and grouped along four main initiatives:*** (i) upgrading the empirical modeling and testing it with various policy scenarios and maintaining a larger disaggregated database that covers economic sectors beyond the central government; (ii) revisiting and updating the existing MTFF on a regular basis[18], leading to the preparation of a Medium Term Budget Framework (MTBF); (iii) preparing a Budget Framework Paper to be incorporated as part of the annual budget preparation cycle and develop capacity to formulate policy reports for senior management on various economic and fiscal issues; and (iv) developing an institutionalized macro-fiscal specific training program aligned with the target institutional and regulatory framework of the MFD and the budget directorate.

Sub-component 1.2: Public Debt Management (US$0.353 million)

26. ***The activities under the Public Debt Management sub-component reflect the progress made under EFMIS, specifically the creation of the PDD, the developing of a medium term debt management strategy, and the upgrade and strengthening of the relevant back office function.*** Going forward, the objective of FMR 2 is to consolidate capacity, gradually expand the scope and functions for debt management, and strengthen the operational aspects of the department.

27. ***To achieve these objectives, activities under this sub-component will focus on the following areas:*** (i) debt management strategy development and cost-risk analysis, including building tools to analyze risk, (ii) debt management strategy implementation, including supporting the development of an effective and transparent primary market for government securities, (iii) organization and staffing of PDD, including operational risk management, strengthening the front office function, and the development of detailed and targeted training programs, (iv) reporting, both internal and external, and the establishment of a dedicated investor relations function, (v) management of contingent liabilities, and (vi) a review of the legal framework for debt management.

Component 2: Public Expenditure Management (US$3.248 million)

Sub-component 2.1: Expenditure Programming & Budget Preparation (US$0.595 million)

28. ***The MoF has adopted new budget preparation guidelines[19], and introduced the GFS 2001 classification and a MTFF in the budget circular.***[20] The MoF has taken a decision to

[17] This include a variety of activities (e.g., hands-on training, study tours, workshops, e-learning, etc.) delivered in-house or by third parties.
[18] This could be on a quarterly or bi-annual basis.
[19] Such as costing parameters, tackling budget transfers, and others.
[20] All introduced with support from EFMIS project.

implement these changes to the budget process starting from the 2014 budget rounds. As a result FMR 2 will provide hands-on training on budget preparation techniques to support implementation. The sub-component would also support further enhancements to the budget preparation practices including refining the guidelines and parameters of budget circulars, engaging line ministries on implementation, and revisiting the budget calendar.

29. ***The sub-component proposes to revisit the institutional framework of the budget directorate, design a new organization structure, and implement such restructuring as to align the functions of the directorate with the new legal framework (i.e. the new draft budget systems law, GFS 2001 Classification*[21]*) and its primary role in expenditure programming and budget preparation.*** This further entails providing extensive training for budget officers to work with line ministries[22] on the envisaged reforms to adopt the new system and work towards minimizing irregularities and widening the comprehensiveness of the budget. A focused engagement plan will be developed and carried-out with line ministries, on pilot basis, to ensure proper implementation of these new budget preparation processes.

Sub-component 2.2: Budget Execution (US$1.996 million)

30. ***On-going challenges for budget execution include*** (i) inefficient (or sometimes lack of) processes and procedures; (ii) certain capacity constraints in MoF and inadequate capacity to implement budget execution reforms in line ministries; (iii) lack of information systems capability and capacity to support either existing and/or new functions; (iv) substantially understaffed and insufficiently equipped IT department; and (v) lack of automation of data flows between MoF units internally. As part of the implementation of the PFM reform strategy and building on the outputs from EFMIS, FMR 2 activities will address the aforementioned gaps. This will be done through the provision of technical assistance, mentoring and training, and limited IT hardware.

31. ***FMR 2 will provide technical advisory support and training for the MoF to enhance the budget execution processes and practices notably treasury and cash management, transition to centralized Treasury Single Account operations, enhanced commitment controls and liquidation, and improved accounting practices and reporting based on new budget classification and a new chart of accounts.*** Through MoF, technical assistance will also be provided to selected line ministries to improve cash planning and enhance the control environment.

32. ***These activities will be complemented by a two-tracked approach for strengthening the IT systems.*** The first track focuses on working towards stabilizing the existing IT system through providing training on COBIT IT governance framework, procuring a basic data warehouse system to improve reporting capabilities, and supporting "quick fix" solutions for programming the implementation of IPSAS cash-based accounting standards, BDL transfer data on cash figures to MoF, and other data flow stabilizing applications. The second track provides technical assistance

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[21] A new draft budget system law has been prepared by MoF with support from EFMIS to replace the outdated 1963 Public Accounting Law. The draft has been discussed extensively within the Ministry and with other stakeholders including the court of accounts and awaits Parliament's confidence vote of the newly formed Government. The process of adopting this law is expected to be lengthy especially since it is expected to take substantial discussions at Parliament. The FMR 2 project will support the implementation of this law if approved within the timeframe of this project.
[22] And government agencies, if needed.

for the production of technical and functional requirements and a complete bidding package for the eventual procurement of a modern integrated GFMIS.[23]

Sub-component 2.3: Public Procurement Reforms (US$ 0.305 million)

33. ***The Council of Ministers has endorsed a new draft law in November 2012 tasking the Central Tender Board (CTB) with managing public procurement.*** The CTB new tasks include proposing public procurement legal and regulatory texts, preparing standard bidding documents, training competent personnel for conducting public procurement, and creating and managing a database on all public procurement contracts and render the information available to all parties falling under its jurisdiction.[24] FMR 2 will support CTB to deliver some of those tasks. The objective is to support public procurement reforms initiatives as to modernize and improve the transparency of budget execution and preparation functions. The proposed assistance focuses primarily on improving procurement planning and cost estimates, improving data collection to support budget forecasting simplifying access to public procurement opportunities, and compiling regulations and rules under one platform. More precisely, activities under this component would include (i) supporting the development of a website platform for procurement; (ii) revising procurement manual and standard bidding documents and developing sector specific standard bidding documents; and (iii) strengthening the CTB and concerned stakeholders' capacity through specialized training on procurement international best practices.

Sub-component 2.4: Internal Control and Internal Audit (US$0.352 million)

34. ***The internal control framework in the public sector is currently weak while internal audit functions are absent.*** This leads to increased risks for misuse of public funds. In response to the Government's efforts to increase transparency and accountability of the internal financial controls over budget execution, FMR 2 will support the initiation of new internal control and internal audit processes within MoF on a pilot basis. This will be pursued through identifying and monitoring risk management practices, and creating an independent and objective internal audit and assurance function. Such support is expected to reduce the risks of improper utilization of public funds, fraud, waste and corruption. It is also expected to improve the overall efficiency and effectiveness of MoF budget operations.

35. ***More precisely, activities under this sub-component include:*** (i) a consolidation of existing diagnostic reviews, and mapping of the internal control framework at MoF, (ii) establishing an MoF interdepartmental control and audit working group, (iii) piloting an operational Internal Audit function within MoF, and (iv) raising awareness, knowledge, and training for civil servants. In this respect, FMR 2 will coordinate with the EU twinning project on developing and implementing the Public Internal Financial Control framework, applied in many EU-member countries.

[23] Government Financial Management Information System. Based on the successful convergence of the two parallel tracks, an overall institutional assessment of MoF will be conducted at the conclusion of FMR 2 to determine the feasibility of a follow-up GFMIS project using the completed procurement package.
[24] The CTB authority encompasses public administrations, municipalities and autonomous public agencies.

PROJECT FINANCING

Lending Instrument

36. ***Investment Project Financing is the instrument most suitable for the financing of the project.*** This is due to the flexibility such financing mode provides to support the creation, rehabilitation, and maintenance of economic and institutional infrastructure. This is particularly the case of FMR 2, which is designed to finance consultant services and training programs in support of the Government's comprehensive PFM reform agenda.

Project Cost and Financing

37. ***The total project cost is US$5.2 million. It will be fully financed by an IBRD loan.*** The breakdown of the project costs among the two components and their related sub-components is shown in the table below. The project does not envisage any Government counterpart funding or donor financing.

Project Components	Project cost (US$)	IBRD or IDA Financing (US$)	% Financing
1. Macro-Fiscal Analysis and Public Debt Management	968,222	968,222	100
1.1. Macro Fiscal Analysis	614,680	614,680	100
1.2. Public Debt Management	353,542	353,542	100
2. Public Expenditure Management	3,247,943	3,247,943	100
2.1. Expenditure Programing and Budget Preparation	595,340	595,340	100
2.2. Budget Execution	1,995,516	1,995,516	100
2.3. Procurement Reforms	305,400	305,400	100
2.4. Internal Control and Internal Audit	351,687	351,687	100
Project Management Unit	723,040	723,040	100
Total Baseline Costs	4,939,205	4,939,205	100
Physical contingencies	260,795	260,795	100
Price contingencies	0	0	100
Total Project Costs	5,200,000	5,200,000	100
Interest During Implementation	0	0	
Front-End Fees	0	0	
Total Financing Required	**5,200,000**	**5,200,000**	100

38. ***At the request of MoF[25], retroactive financing will be provided to support the establishment and staffing of the Project Management Unit in the Ministry of Finance prior to the World Bank's Board approval of the loan.*** The retroactive financing will also cover other activities identified under the project's components.

LESSONS LEARNED AND REFLECTED IN THE PROJECT DESIGN

39. ***Lessons learned from the EFMIS project have been incorporated in the design of FMR 2 activities.*** These lessons essentially draw on the risks faced during the five years of EFMIS implementation. The most important lessons can be summarized below:

[25] Ministry of Finance Letter entitled "Retroactive Financing on Lebanon Fiscal Management Reform Project (LFMR) project", number 1915/S1, dated 17 May 2013.

Flexible approach to reforms: the political fragmentation in Lebanon has proven to be a constraining factor for PFM reforms. As a result of political deadlock many crucial administrative, regulatory, and legislative decisions related to public finances have been pending or took extensive time to be adopted; notably the approval of a budget law and the hiring of qualified and specialist staff at MoF. All of this has delayed deliverables under EFMIS. As a result, the FMR 2 design takes a flexible approach in which reforms are steadfastly driven in windows of favorable and opportune political environment.

Incubation-type model: EFMIS had used an incubation-type model in its engagement with MoF where international and local experts have worked on a frequent basis with working groups of civil servants from within the Ministry as to implement the planned reforms under each of the project's component. Prior to implementation, these working groups would participate in the design of solutions through extensive rounds of consultations. This hands-on and focused approach has proven to be successful in accelerating deliverables and is therefore embedded in the new project design.

Sequencing of activities and on-the job training: the wide scope of PFM reforms endorsed by EFMIS has been faced with limitations in the absorptive capacity of MoF. This primarily came as a result of low capacity in areas such as policy analysis functions, and difficulties in hiring civil servants with the right set of skills to fill critical vacancies across many departments within MoF. To deal with these issues the project recurred to: (i) sequence the activities to improve implementation; and (ii) provide extensive on-the-job training for MoF staff as to compensate for mismatches in personnel skills or academic background. This was successful in EFMIS and is also embedded in the activities of FMR 2.

IV. IMPLEMENTATION

INSTITUTIONAL AND IMPLEMENTATION ARRANGEMENTS

40. ***The Ministry of Finance, as the loan recipient, is the project's implementing agency and will oversee the implementation of all the FMR 2 activities.*** MoF will also have the primary responsibility for ensuring the Bank's guidelines and procedures are adhered to. To facilitate the comprehensive and continuous oversight, MoF will establish a Project Management Unit (PMU), financed by the loan proceeds, with primary responsibility for daily project implementation and coordination of activities under the project's components.

41. ***The Project Management Unit will be comprised of four full-time dedicated staff.*** A project manager will be serving as the key interlocutor for the Bank and ensuring consistency between the beneficiary departments within the Ministry and other stakeholders. The project manager will be supported by a Financial Officer, a Procurement Officer, and a Project Assistant. The Financial Officer and Procurement Officer will be managing the daily financial management and procurement activities of the project, while the Project Assistant will provide administrative support to the PMU. Financial management and procurement arrangements are outlined in subsequent sections and in further details in Annex 3.

42. ***The FMR 2 implementation arrangements build on the modalities of engagement outlined in the EFMIS project.*** The MoF has built expertise and know-how in managing and executing similar PFM reform projects after the successful implementation of EFMIS. This

provided them with some knowledge and relevant experience in implementing World Bank guidelines and procedures. As a result, MoF senior management has requested to maintain a similar engagement framework in the upcoming FMR 2. Therefore the project will finance consultants to provide technical assistance and training for MoF staff, or other relevant stakeholders, on the identified reform components. It will also finance some IT equipment and software, as outlined in the procurement plan, dated July 15, 2013. The PMU will coordinate these activities in collaboration with the PFM reform steering committee that will act as the technical counterpart. The Minister and Director General of MoF will play a strategic guidance role.

43. ***The successful implementation of the project hinges on the coordination of all stakeholders involved in the PFM reform process.*** While the PFM reform steering committee coordinates activities within MoF, the relationship between MoF and other stakeholders is determined through existing laws and regulations. The project aims to strengthen these linkages; examples include: (i) the BDL and MoF discuss public debt management through the High Debt Committee; (ii) the Public Accounting Law organizes the control framework between Courts of Account, Central Inspection and the Public Accounting Directorate at MoF; and (iii) CDR cooperation with MoF is regulated through various Memoranda of Understanding. The project is also supporting a restructuring of the Budget Directorate that strengthens the linkages with line ministries through the sectoral budget officers.

44. ***In order to ensure the project is being implemented in a manner consistent with the GoL's overall reform efforts, the PMU will be overseen by the MoF and the Minister of Finance will be regularly informed of progress under the project and consulted as needed.*** The World Bank will provide implementation support. The Bank will monitor the project's deliverables, provide no-objection on the various activities, and engage with MoF's senior management, technical staff, PMU and project consultants to advise on the direction and priorities of the reforms.

RESULTS MONITORING AND EVALUATION

45. ***Monitoring and Evaluation (M&E) capacity in Lebanon is weak and no country system is currently in place to monitor PFM reforms.*** Therefore the project cannot resort to such country system to monitor the identified intermediate results indicators. The project will resort to existing data sources especially fiscal and budgetary data currently available. Improvements have been made on this front especially in terms of capturing disaggregated fiscal and public debt data that are largely consistent with IMF standard classification. The FMR 2 project will also be financing an IT data warehouse and other IT stabilizations that will increase significantly the reporting capacity of the Ministry. While these technological improvements will help to improve the quality of information received; nonetheless, faced with the above structural constraints, the PMU will have to play an important role in M&E.

46. ***The PMU will be responsible for monitoring the daily project implementation. The PMU will prepare quarterly progress reports, including updates on the indicators identified in the results framework (Annex 1).***

SUSTAINABILITY

47. ***The Ministry of Finance's strong level of ownership for the project enhances the sustainability of the proposed PFM reforms.*** Such commitment is highlighted through tangible MoF measures related to enhanced strategic orientation, structural reforms including legislative and regulatory changes, organizational restructuring, and institutional capacity. Below are indicative actions on the sustainability of the PFM reforms:

a. MoF engagement with the World Bank on PFM reforms since 2009, with EFMIS, and their request for a follow-up project - FMR 2 - that continues with the earlier areas of reforms and has similar modalities of engagement.
b. The formal adoption of forward looking medium term strategies on debt management, PFM reforms, and budget execution reforms roadmap.
c. The establishment of a PFM reform steering committee, representing all departments within MoF, tasked with implementing the PFM reform strategy. The committee will also act as a technical counterpart for the project.
d. The creation of new departments such as the macro-fiscal department and the restructuring of existing ones notably the public debt directorate and cash management department. The new project intends to go further to support alignment of reforms with the functions of the Ministry notably at the level of the budget department, treasury and public accounting directorate.
e. Extensive capacity building activities and on-the-job training are planned for civil servants as part of the new project. The expansion of the PFM training strategy[26], envisaged by FMR 2, will be a cornerstone to institutionalize a training policy within MoF allowing for regular capacity building for all Ministry staff at different levels and responsibilities.

V. KEY RISKS AND MITIGATION MEASURES

RISK RATINGS SUMMARY TABLE

Stakeholder Risk	**Moderate**
Implementing Agency Risk	
- Capacity	Substantial
- Governance	Substantial
Project Risk	
- Design	Moderate
- Social and Environmental	Low
- Program and Donor	Moderate
- Delivery Monitoring and Sustainability	Substantial
Overall Implementation Risk	Substantial

[26] The training strategy developed for MoF is a deliverable of the EFMIS project.

OVERALL RISK RATING EXPLANATION

48. ***The project faces different set of operational risks that might constrain the deliverables outlined in this project***. These implementation risks are outlined below (refer to Annex 4 for a comprehensive description of risks surrounding the operation):

a. *Absorptive Capacity and Staffing:* while MoF has developed some know-how in implementing such types of projects, addressing staffing gaps and mobilizing human resources remains a key implementation risk for MoF and other stakeholders (e.g line ministries). Also further capacity building will be needed in order to absorb the wide scope of reforms put forward by FMR 2. To address these concerns, the new project is proposing to roll-out a training policy and plan that systematically provides capacity building for staff on relevant topics. The plan will identify the modality of training needed whether they are courses, on-the-job coaching, external training or other, with the project executing part of it. On the other hand, the sequencing of activities will also be considered. Being close to the client allows the FMR 2 team and advisors to identify rational implementation plans under each sub-component that take into account the staffing and capacity of involved departments. This will be done at the inception stage of each sub-component and during the initiation of various activities.

b. *Institutional Risks:* Despite the fact that the project is less exposed to the complex political context of the country, implementation risks remain as executive and regulatory decisions are still needed to push PFM reforms forward. One of the most significant risks is the further delay in the approval of a budget law without which the outcome of PFM reforms is attenuated and less visible for the public. With prospects currently low for adopting the annual budget law, the implementation of EFMIS milestones gain significant importance to ensure a smooth implementation of FMR 2. This comes as a result of the inter-linkages between the two projects. Progress on those milestones[27] has been significant with deliverables were submitted, as planned, by September 2013. This will mitigate some of the political volatility risks as it removes the dependency of FMR 2 tasks on policy decisions.

c. *Donor Coordination:* amidst several donor funded PFM support projects - including EU, IMF-METAC, UNDP and the World Bank - it will be important for MoF to play a stronger coordination role. Sub-optimal coordination increases the risks of overlapping activities leading to inefficient use of resources and client burdening. However, a strong coordination and MoF ownership can create valuable synergies between the different projects, drawing on the comparative advantage of each donor and therefore maximize the returns of such interventions. To mitigate this risk, the PFM reform strategy formulated and adopted by MoF will constitute the guiding document for reforms to be supported. Also, the PFM reform steering committee, recently created, is expected to be tasked with overseeing all donor-financed projects. On the other hand, the World Bank and the PMU of FMR 2 will constantly share updates with donors on activities to be performed under the project.

[27] These milestones include (i) the formulation of medium term macro fiscal framework and debt strategy, (ii) the adoption of the amendments to the public accounting law, (iii) the implementation of the GFS 2001, and (iv) the finalization of the IT audit.

VI. APPRAISAL SUMMARY

ECONOMIC AND FINANCIAL ANALYSES

49. ***FMR 2 is expected to have a high development impact on PFM in Lebanon. As a technical assistance and capacity building project it is difficult to quantify a precise economic rate of return for this operation.*** This limits the ability to carry out an economic and financial analysis. The project costs are expected to be comparable, to a large extent, to the EFMIS project. However, since the project invests in technical assistance, training and selected information technology improvements that tackle PFM practices and processes, it is expected to result in improved public resource management, and potential fiscal savings. This yields development benefits for the country in the medium and long run. The major channels of such returns can be highlighted below:

a. MoF will institutionalize and strengthen its policy analysis capabilities, feeding into better informed policy decisions and consequently pushing towards improved fiscal policy and fiscal outcomes.
b. The processes governing budget related operations will be strengthened to comply with international best practices. This leads to increased internal transparency, improved communication, and strengthened strategic orientation in the budget preparation cycle. This pushes for further efficiency in the allocation and use of public resources.
c. The formulation and implementation of a comprehensive debt management strategy coupled with improved debt recording capabilities, better investors' relationship, and the organization of debt issuance processes are expected to reduce debt related risks and costs as debt structure and maturity profiles improve.
d. Strengthening cash management and cash planning coupled with efforts to streamline the process from commitments to liquidation will have a positive fiscal impact especially in reducing borrowing needs.
e. FMR 2 activities will support the introduction of an internal control and internal audit framework that could be used as a pilot to be replicated in line ministries. This would contribute to improved fiscal governance in the country.
f. The successful implementation of PFM reforms supported by FMR 2, including the IT related activities, will bring the MoF a step closer to the adoption of an integrated financial management information system.

50. ***Cumulatively, the institutional and structural reforms brought forward by the project contribute to improve the governance of the PFM sector.*** By implementing the PFM reform plan, the project contributes to ensuring a more efficient allocation of public money. As such, FMR 2 contributes to improving governance and internal transparency especially with the introduction of checks and balances in the budgetary process. FMR 2 also offers extensive capacity building geared towards civil servants to strengthen the core competencies of the public administration. The project looks to institutionalize such training as to enable the administration to sustain reforms and take it to the next level. The combination of improved budgetary practices and increased civil service competencies are important to ensure the overall accountability of Government despite the complex political economy factors in Lebanon.

51. ***The World Bank's extensive experience in the design and implementation of PFM projects adds value to the Lebanese reform process.*** In addition to financing international

expertise, FMR 2 provides significant capacity building support to MoF, also to manage the complex political economy of PFM reforms in Lebanon. The project also creates important synergies with other donor support programs, mainly through the advisory and capacity building support that will generate important input for other donor programs.

TECHNICAL

52. ***The proposed technical design of the project has been agreed with the GoL and is considered as the most appropriate to build capacity and support the implementation of the PFM reform plan.*** Reforms identified under each sub-component will be driven and implemented by the relevant departments or working group within MoF or other stakeholders. These reforms are guided by dedicated international advisors foreseen and financed through FMR 2. This replicates the successful modus operandi followed during the EFMIS project. Indeed the MoF officials are increasingly observing the value of this incubation-type model where the development of various ministerial departments and working groups is enhanced by on-the-job coaching of both experienced international advisors and the FMR 2 team. Such close presence enables the project to design efficient tools to build the civil servants capacity and help push for the highest returns on PFM reforms.

53. ***The project design features help mitigate the risks of political volatility and frequent government changes. These features are summarized below:***

- The PFM reforms steering committee will act as a technical counterpart. This committee is formed of senior managers representing various MoF budget functions and will ensure the continuity of reforms as well as the institutional memory of the project.
- The project takes a flexible approach for reforms where further activities and deliverables will be pushed if the political environment is conducive for reforms. This might entail some re-allocation of funds within or throughout components. Such two-tiered design was adopted by the Lebanon CPS and comes as lessons were drawn during EFMIS implementation.

FINANCIAL MANAGEMENT

54. ***An assessment of Financial Management (FM) systems within MoF has identified the following risks to be mitigated: limited human resources with experience in Bank-financed projects; limited capacity of the MoF current accounting information system to capture all transactions and generate the required project financial reports; and limited procedures regarding FM implementation of donors' project and absence of an internal audit function.*** To mitigate these risks, the following is proposed: (i) MoF to update the Project Operation Manual (POM) used by EFMIS, including the FM chapter, and use it as the operation manual for this project; (ii) hire a financial officer as part of the PMU tasked with handling the project's FM arrangements and ensure compliance with the POM; (ii) use the existing EFMIS project accounting software to record project daily accounting transactions and generate the required quarterly Interim Unaudited Financial Reports (IFRs) as per World Bank reporting requirements. With these actions the proposed FM arrangement will satisfy the minimum requirements under OP/BP 10.00.

55. ***The project is required to issue quarterly IFRs and annual Project Financial Statements (PFS) for submission to the World Bank prepared in accordance with IPSAS[28]-cash basis standards.*** These will be sent to the Bank respectively by no later than 45 days after the end of each quarter and six months after the end of each fiscal year, respectively.[29] To ensure that funds are readily available for the project implementation, MoF will open and operate a Designated Account (DA) in US dollars at the BDL, and MoF through the PMU will maintain this Designated Account. Deposits into, and payments from the DA will be made in accordance with the provisions stated in the loan agreement and as outlined in the World Bank "Disbursements Guidelines for Projects".

56. ***The PFS will be audited by an independent private external auditor acceptable to the World Bank.*** The audit TORs was finalized and agreed upon with the Bank during negotiations. The audit report and management letter will be due six (6) months after the end of each fiscal year. According to the Bank's disclosure policy and per the requirement OP/BP 10.00, the project's audited annual financial statement will be made available to the public. Details of the FM arrangements are found in Annex 3.

PROCUREMENT

57. ***A procurement capacity assessment of MoF was conducted to identify risks and mitigation measures.*** To reduce the identified risk, the following measures are proposed: (i) include in the ToRs of the project's audit a review on the time taken to provide procurement decisions and the time needed to make justifications when those decision are over-rided; (ii) agree on a relevant training program to be implemented during the project; (iii) provide appropriate support[30] to prepare a detailed procurement plan with clear linkages to the PDO; (iv) prepare acceptable sample bidding documents for National Competitive Bidding; (v) ensure clear and quantifiable evaluation criteria and monitor compliance; (vi) set deadlines for complaints submission and for decision making by the MoF; (vii) establish a system to monitor and expedite contract modifications or change orders and include this requirement as part of the TOR for procurement audits; (viii) agree on appropriate publication of procurement decisions.[31]

58. ***The following project procurement arrangements will be envisaged:***

a. Project guidelines: World Bank Procurement and Anti-corruption guidelines are applied for the project.[32]
b. Procurement methods for goods and non-consulting service: the project is expected to conduct international competitive bidding, national competitive bidding, shopping, framework agreements, and direct contracting.
c. Selection of consultants: the project is expected to conduct quality and cost based selections, selection under a fixed budget, least-cost selection, selection based on the

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[28] International Public Sector Accounting Standards.
[29] Project Fiscal year ends December 31st.
[30] Staff, training, and tools.
[31] e.g. on a website or press bulletin.
[32] Refer to Annex 3 for a complete list of these guidelines.

consultants' qualifications, single source selection, and selection of individual consultants including sole sourcing procedures.[33]

d. procurement plans: An initial procurement plan, dated July 15, 2013, for the life of the project has been developed by MoF. It defines the prior review and procurement methods thresholds. It will be updated by MoF and reviewed by the Bank at least twice a year or as seen necessary.

e. Frequency of implementation support missions and post procurement reviews is foreseen respectively twice and once yearly.

Further details on Procurement arrangements are found in Annex 3.

SOCIAL AND ENVIRONMENT (INCLUDING SAFEGUARDS)

59. ***FMR 2 is classified as a "Category C" project and does not trigger any environmental or social safeguards.*** FMR 2 project aims to build fiscal policy analysis capacity, improve the budgetary allocation of public resources, enhance the efficiency of the government financial management systems, and tighten the control environment for more effective use of public resources. As such, the project finances capacity building, technical assistance, training, and advisory services for the Ministry of Finance and other government stakeholders. These activities do not include any physical infrastructure. No new building are to be constructed, only some potential limited upgrades of existing computer rooms might be required before installing some of the IT systems or equipment supported through project. Therefore, this is not expected to have any environmental impact. Additionally, the project does not focus on any particular population group or social programs, and does not call for any resettlement.

[33] In view that the first project (EFMIS) design was found satisfactory, it is anticipated that the project may retain individual consultants already identified competitively.

ANNEX 1: RESULTS FRAMEWORK AND MONITORING

LEBANON: Fiscal Management Reform Project 2*

Project Development Objective (PDO):
The objectives of the Project are to strengthen the Recipient's capacity in fiscal policy analysis, debt management, and budgetary allocation of public resources; enhance the efficiency of the Recipient's financial management systems; and tighten the control environment for more effective use of the Recipient's public resources.

PDO Level Results Indicators*	Core	Unit of Measure	Baseline	Cumulative Target Values** YR 1	YR 2	YR3	Frequency	Data Source/ Methodology	Responsibility for Data Collection	Description (indicator definition etc.)
Budget Framework Paper developed and submitted for cabinet discussion prior to the issuance of budget circular		Yes/No	No	No	No	Yes	Annual	MFD	PMU	Develop a Budget Framework Paper that outlines the budget's strategic policies and priorities and the related financing plan for the medium term, and spells out government financing plans and fiscal targets for medium term using the MTFF framework.
Domestic borrowing plans are formulated and published on an annual basis by the PDD		Yes/No	No	Yes	Yes	Yes	Annual	Domestic borrowing plans are made publicly available	PDD (in close cooperation with BDL)	A consistent and transparent approach to strategy implementation through a well working primary market for gov't securities ensures access to low risk funding

Line ministries with detailed budgets prepared on time and as per MTFF guidelines.		Number	0	0	2	5	Annual	Budget Directorate & PMU	Budget Directorate & PMU	Line ministries budgets prepared per MTFF, and negotiated & discussed technically between to-be-appointed budget officers at MoF and counterparts.
MOF financial statements issued in compliance with IPSAS cash standards		Yes/No	No	No	No	Yes	Bi-annual and on- going assessments with achievement in year 3	MoF Accounting Directorate Treasury Directorate	MoF Accounting Directorate Treasury Directorate	To begin at the start of next FY (Jan 2014). All government financial statements issued by MoF to be in compliance with IPSAS reporting standards in year 3. Pre-conditions are IT system ready to host new accounting procedures (Chart of Accounts) and implementation of Chart of Accounts.
Annual internal audit report issued by the MOF and approved by the relevant authority as defined by decree		Yes/No	No	No	Yes	Yes	Annual	MOF	PMU	The internal audit function established will issue internal audit report and will submit them for relevant authority's

										approval
Number of trained staff of which females		Number Percentage	0 0	20 50	40 50	60 50	Annual	MoF and CTB	PMU	Number of MoF, CTB and other stakeholder staff trained throughout the project of which 50 percent are females
**Due to the nature of the project, the project will directly benefit the limited number of staff of respective Government institutions through training and TA while the rest of the population will benefit indirectly. Therefore, a core mandatory indicator "Direct project beneficiaries (number), of which female (%)" is not included in the results framework.*										
INTERMEDIATE RESULTS										
Intermediate Result (Component 1.1): Macro-Fiscal Analysis										
General forecasting and policy scenario reports produced by the MFD		Number	0	1	2	4	Annual	MFD	PMU	Use MTFF and later MTBF to develop various short policy reports on an ongoing basis throughout the Lebanese fiscal year.
Staff trained on macro-fiscal themes as per the new training program		Number	0	0	7	15	Annual	MOF	PMU	Staff trained as the training policy. To include MFD staff, other budget directorate staff and counterparts in external entities if deemed necessary.
Intermediate Result (Component 1.2): Public Expenditure Management										
Annual analytical reports on debt and risks issued by the PDD using data from the newly installed DMFAS debt recording system.		Yes/No	No	No	Yes	Yes	Annual	PDD	PMU	Internal and external reports, including analytical reports, strengthen governance and

										accountability. A precondition for good reports are high quality data – in this case provided by the DMFAS debt recording system.
A medium term debt management strategy is published on an annual basis. From year 3, the scope of the debt management strategy is expanded to include policies regarding managing contingent liabilities.		Yes/No	No	Yes	Yes	Yes	Annual	PDD	PDD	The medium term debt management strategy is expanded to include contingent liabilities, and policies regarding guarantee issuance, pricing etc., are developed.
Intermediate Result (Component 2.1): Expenditure Programming and Budget Preparation										
Sections of the Institutional framework for the Budget Directorate developed and approved		Text	None	3 sections developed approved & rendered operational: Orga. structure, governance model & the manpower plan	2 new sections (5 as cumulative) developed, approved & rendered operational: Functions provided and the internal & external interaction model	All (5) sections of the institutional framework operational	Annual	Budget Directorate & PMU	PMU	Develop a new organization structure and manpower plans, and revisit functions, job descriptions and the governance and interaction model
Intermediate Result (component 2.2): Budget Execution										
Number of inactive public administration accounts		Number	32 accounts	27	16	0	Annual	MoF and BDL	MoF Treasury and Cash	Based on public administration

(maintained by Treasury)			(2013)						Management Directorate (CMD)	(i.e., line ministries) accounts under MoF Treasury (Account 36) held in BDL as of June
Reduction of cash collected by LAOs and ACO (Beirut Accounting and Cashier Office)		%	842 billion Lebanese Pounds (2012)	15%	25%	35%	Bi-annual	MoF LAOs and ACO	MoF CMD	Based on average amount of cash collected from 2010-12 (842 billion LBP), there should be a percentage reduction in cash collected for all LAOs and ACO.
Reduction in average time of liquidation-payment for selected line ministries		% (cumulati ve)	2 months (2012)	0%	10%	20%	Bi-annual	MoF Expenditure and Treasury Directorates	MoF Expenditure and Treasury Directorates	Reduction in the average time between selected line Ministry (including Ministries of Health, Social Affairs, Education, and Public Works) submission of liquidation documentation to MoF Expenditure Directorate until receipt of payment. Commitment ceiling should be in place.
Line ministries adhering to MOF-issued commitments ceilings based on cash plans		Number	0	0	2	4	Annual	MoF Accounting Directorate	MoF Accounting and Budget	The expectation is that these ministries will

								and Budget Directorate	Directorates	be Ministries of Health, Social Affairs, Education, and Public Works. MoF to (a) issue commitment ceilings based on ministries' cash plans; and (b) monitor that these ministries are in compliance. To apply commitment ceilings, MoF will need a decree or passage of law. Currently, there are no ceilings for commitments based on cash plans so ministries can enter into commitments against entire budget allocation rather than prescribed ceilings.
GFMIS procurement package completed		Yes/No	No	No	No	Yes	Annual	MoF	MoF	By year 3, key institutional reform and capacity development should be in place to establish the foundation for a future GFMIS. This will be

										evidenced by a completed GFMIS procurement package (i.e., tender documents prepared and ready).
Intermediate Result (component 2.3): Public Procurement Reforms										
Bids advertised using the new procurement portal		Number	0	0	200	400	Annually	CTB procurement portal	CTB	The total number of bids advertised on the new procurement portal at CTB.
Institutions using standard bidding documents		Number	0	0	3	6	Annually	CTB	PMU	The total number of additional institutions (line ministries or government agencies) adopting the standard bidding document.
Intermediate Result (component 2.4): Internal Control and Internal Audit										
MOF interdepartmental control and audit work force established, fully staffed and operational		Yes/No	No	Yes	Yes	Yes	One time	MOF	PMU	The established internal controls and audit working group staff will carry on the recommendations as per the consolidated report to strengthen the internal control environment at MOF.

ANNEX 2: DETAILED PROJECT DESCRIPTION

LEBANON: Fiscal Management Reform Project 2

Component 1: Macro-Fiscal Analysis and Public Debt Management (US$0.968 million)

Sub-component 1.1: Macro-Fiscal Analysis (US$0.615 million)

1. ***Macro-fiscal analysis was absent from the core functions of the Ministry of Finance prior to 2012.*** This function was partially assumed by a team of advisors in coordination with other MoF departments who provided the required data. This arrangement remained sub-optimal as capacity and institutional memory were not built within MoF. As part of the EFMIS project, a macro-fiscal department (MFD) was created in March 2012 with the objective of carrying out those analysis functions. The MFD team, now composed of 7 MoF staff, has received on-the-job training and has produced reports including a basic macro-fiscal forecasting exercise and a medium term fiscal framework (MTFF).

2. ***Despite these positive developments, the MFD lacks experience.*** This young team that until a year ago was not exposed to macro-fiscal issues is facing a workload that will increase in volume and complexity. The team would thus need to be empowered and trained to reproduce and maintain the forecasting model and the MTFF, expand the database, and analyze and prepare policy impact notes. The development of a fully operational, effective, and innovative MFD is a long-term engagement that requires strong MoF management ownership and continuous external support.

3. ***The objective of this sub-component is to build on previous developments and transform the MFD into the policy analysis unit of the Ministry.*** The immediate (low-level) objective is to maintain the positive impetus recorded to date and expand the scope and the depth of operations. This can be achieved by continuing coaching and by systematic capacity building with diverse tools[34] delivered in-house or by third parties.[35] The training will be complemented by a steady increase in the work plan to acquire the required skills to deliver the needed macro-fiscal analyses and reports and ultimately transform MFD into a self-reliant unit. To achieve the stated objectives, a number of activities are envisioned and grouped below along four main initiatives.

4. ***Upgrading the empirical modeling and maintaining a larger database: A basic macro-fiscal forecasting model was developed under EFMIS based on a database that was designed and populated.*** Moving forward, the work will build on this initiative, on one hand widening and disaggregating the database, and on the other, upgrading the model and testing it with policy scenarios. On the database front, the work will include formalizing the relationship with data providers to ensure regular and timely sharing of data and expanding coverage to add and disaggregate sectors of the economy. On the forecasting model front, the work will include rolling over the model taking into account the expanded database, and run policy scenarios including debt sustainability analysis to feed senior management with informed policy advice.

[34] e.g., study tours, workshops, e-learning, etc.
[35] such as the Basil Fuleihan Institute of Finance.

5. ***Revisiting the MTFF leading to the preparation of a MTBF: under EFMIS the MFD has developed the first version of an MTFF, feeding directly into the 2013 budget circular.*** Activities going forward encompass the timely and frequent update of the MTFF, and its expansion as to include additional policy variables. Utilizing the MTFF, the MFD will work closely with the budget officers on preparing an MTBF in cooperation with selected line ministries.

6. ***Developing policy reports and a Budget Framework Paper: The MFD has over the course of 2012 assumed the lead role in re-producing some reports, previously prepared by the UNDP unit.***[36] Looking forward, FMR 2 will provide training and mentoring for the MFD to enhance the scope and analytical content of these reports to cover fiscal and economic performance, revenue performance, and spending forecast. Additionally and as part of strengthening the budget preparation process, technical assistance will be provided for developing a Budget Framework Paper. This policy note, prepared in collaboration with the budget directorate, engages line ministries on government strategic priorities amidst the overall fiscal framework set by the MTFF. It is expected to be submitted for cabinet discussion and endorsement prior to the issuance of budget circulars.

7. ***Developing and implementing an in-depth training policy: to institutionalize the training function within MoF and avoid ad hoc interventions, FMR 2 will support the formulation of an in-depth macro-specific training policy.*** This policy builds on the general training strategy developed under EFMIS and will be implemented for all civil servants involved in macro-fiscal work. To do so, the project will fund a training expert(s) to formulate a policy that (i) identifies training activities, training tools, and service providers; (ii) develops, sequences, and customizes training modules; (iii) works with various stakeholders to institutionalize and implement the training policy and the associated activities.

Sub-Component 1.2: Public Debt Management (US$0.353 million)

8. ***The activities under the Public Debt Management sub-component reflect the progress made under EFMIS, specifically the creation of the Public Debt Directorate (PDD), the developing of a medium term debt management strategy, and the upgrade and strengthening of the relevant back office function especially with the installation of the DMFAS debt recording system.*** Going forward, the objective of FMR 2 is to consolidate capacity, gradually expand the scope and functions for debt management, and strengthen the operational aspects of the department. The specific activities envisaged to achieve this objective are presented below.

9. ***Debt management strategy development and cost-risk analysis: The analytical foundation for the debt management strategy presented to the High Debt Committee in April 2013 was provided by the World Bank-IMF Medium Term Debt Management (MTDS) Analytical Tool.*** The tool served PDD well, and provided a solid analytical basis for the decision on the preferred debt management strategy. Going forward, and in line with international

[36] The UNDP unit is a team of experts hired from outside the civil service on a contractual basis. The unit is funded by the Lebanese Government and managed by the UNDP. Similar units exist in other ministries and agencies and their mandates vary. By and large, they assume the role of an advisory team attached to the Minister, and depending on the internal capacity of the Ministry, they may also take on operational work. At the MoF, the UNDP unit is over 15 years old and has assumed several key functions in the administration including the role of a macro-fiscal unit.

practice, PDD should develop a range of tools/models in-house. This approach ensures complete knowledge of how the models work, but more importantly, will strongly support continued capacity building in PDD. This activity will require external assistance to guide the process, and the acquisition of modeling software/statistical package such as Matlab. Annual updates of the MTDS are expected to be published and detailed model-development plans formulated. The aim is to develop deterministic scenario analysis and stochastic scenario analysis models, all of which will provide input to detailed borrowing strategies.

10. ***Debt management strategy implementation: implementing the debt management strategy primarily takes place through issuance of new debt, domestically as well as externally.*** For debt issued in the domestic market, a well working primary market is essential for ensuring access to borrowing at fair market prices. This includes a systematic and transparent approach to domestic borrowing. PDD may also consider liability management operations such as buy-backs of securities before original maturity, or swapping interest rate or exchange rate exposure. Liability management operations that are common in mature markets will require that solid processes and procedures are in place, including tools to measure and manage related risks. As such and working closely with BDL, FMR 2 will assist PDD in (i) developing detailed plan for improving transparency and consistency in the domestic borrowing, including borrowing plans, benchmark bonds, primary dealer system (if found beneficial), and liability management operations (ii) implementing a plan for improving transparency and consistency in domestic borrowing, and (iii) developing detailed procedures for Eurobond issuance.

11. ***Organization and staffing on PDD, including operational risk management: according to Law 17, PDD is to be organized along functional lines in a front-, middle-, and back-office, and the law stipulates the number of staff for each function.*** This activity will review the organization structure, including whether a specialized function is needed, and staffing of PDD. It will initially support the establishment of the front-office, but will also include the preparation of detailed job descriptions for each position of PDD, as well as detailed procedures manuals. Based on the detailed job descriptions, training programs for specific staff/functions will be developed. Additionally, the sub-component will develop a strategy for managing operational risks.

12. ***Reporting and investor relations: the publication of the MTDS and borrowing plans are a significant step towards enhancing transparency in debt management.*** To complement this step and strengthen internal accountability and overall governance, FMR 2 will review other existing debt related reports and develop a reporting strategy. The strategy will take into account the current detailed descriptive reports produced on outstanding debt and present ways of substantiating them with stronger analytics. Furthermore, taking into account the high level of activity in issuing bonds in the market, the project will support the creation of a dedicated investor relations group in PDD tasked with external publications and investors' contacts.

13. ***Management of contingent liabilities: the focus of reforms under EFMIS was the direct domestic and external debt.*** A natural next step is to gradually expand the scope to include contingent liabilities, as well as assets and liabilities of state owned enterprises. Information related to outstanding contingent liabilities and their potential risk to the government budget is not collected in a systematic fashion. Also, guarantees are issued without a prior analysis of risk, and charges for issuing these are not linked to the potential risk. Initially, this project component will focus on explicit contingent liabilities (state guarantees), later the scope will be broadened to include the development of policies on monitoring mechanisms for a broader range of contingent

liabilities. As such technical assistance will be provided to (i) review existing (de-facto) procedures to issuing guarantees, (ii) develop framework for issuing and monitoring guarantees, including procedures manuals, (iii) develop clear policies and a formal strategy for issuing guarantees, (iv) develop tools to allow evaluation and pricing of risk to the government related to issuing guarantees, (v) include assets and liabilities of SOEs in the framework for managing contingent liabilities.

14. ***The legal framework for debt management: the legal and regulatory framework for debt management is fragmented and prone to operational risks.*** One example of a challenge under the current set-up is ensuring the adherence to the debt limit when new Eurobonds are issued, since various regulations needs to be checked before each issuance. The activity will provide a detailed review of the current legal framework, including an outline action plan for potential reforms.

Component 2: Public Expenditure Management (US$3.248 million)

Sub-Component 2.1: Expenditure Programming & Budget Preparation (US$0.595 million)

15. ***The process of preparing a budget continues to be based on an outdated 1963 Public Accounting Law.*** Despite notable improvement in the budget processes such as the introduction of the GFS 2001 classification, the formulation of a new budget systems law, the adoption of updated budget preparation guidelines, and the inclusion of an MTFF in the budget circular, further work needs to be done to address a number of gaps.

16. ***The current institutional framework of the budget directorate is not in line with best practices.*** The coordination model with line ministries is still defined by the previous framework and lacks a clear and appropriate communication plan. The Ministry staff is not fully trained to prepare a budget and capacity building activities are not based on a set training policy. The budget, albeit more comprehensive than before, continues to face irregular practices such as treasury advances to ministries, and despite the limitation of the existing legal and institutional framework, there is room for improving the preparation process.

17. ***The work under this sub-component would center on designing an organization structure and governance framework that is in line best practices, with clear functions and processes that includes well trained staff.*** In addition the work aims to better engage and support line ministries and government agencies to adopt the new system and work towards minimizing irregularities and widening the comprehensiveness of the budget. To achieve these objectives, activities are proposed and grouped along four initiatives listed below.

18. ***Revisiting the institutional framework of the budget directorate: the sub-component will help in restructuring the institutional framework of the budget directorate to align its function with the new legal framework.*** Technical assistance will (i) design a new organization structure and develop the required manpower plans to prepare the budget according to the new budget system law, guidelines and international practices[37], (ii) develop new functions and job descriptions, (iii) revisit the budget preparation coordination process both within MoF and with

[37] For instance, create budget officer post who will engage line ministries to develop their own budgets.

line ministries[38,] and (iv) identify and then draft the required legislative amendments to introduce the proposed organization structure. As part of the budget directorate, restructuring will also re-examine the institutional set-up of the MFD including its internal governance, manpower, and reporting mechanism.

19. ***Engaging and coordinating with other government stakeholders: budget preparation reforms under EFMIS were confined to a large extent to MoF.*** Moving forward, FMR 2 will carry out a focused engagement plan with line ministries to ensure that reforms are properly implemented and the quality of budgets submitted by line ministries to MoF improved. The key activities include (i) selecting 3-4 pilot line ministries and assessing their baseline[39], (ii) developing and executing a communication plan highlighting the new reforms (e.g., new budget system law, GFS classification, and the budget ceilings, etc.) and associated changes in processes required, and (iii) providing on-the-job support to the core team in the selected line ministries.

20. ***Developing and executing an in-depth training policy: to implement the new budget systems law and all reforms related to budget preparation, FMR 2 will develop an institutionalized and specialized training policy that provide continuous capacity building activities to MoF staff.*** The target audience includes the teams in charge of budget preparation as well as new recruits or staff realigned to the new budget directorate organization. The engagement will focus on taking stock of the overall training policy developed under EFMIS and identifying training activities and service providers. It will also devise – and implement - specialized training modules and curriculum that will be officially adopted by the Ministry. International experts will be recruited to provide on-the-job coaching as to implement this policy.

21. ***Enhancing the current budget preparation practices and guidelines: technical assistance under this sub-component carries forward the work started under EFMIS to improve the budget preparation processes and guidelines, streamline some procedures, increase transparency, minimize irregularities, and enhance internal capacities and planning.*** This includes (i) developing staff capacity on sectoral issues to strengthen collaboration with line ministries and enhance their analytical capacities to improve the quality of future budgets; (ii) supporting staff in integrating budget requests with MoF internal analysis coming from the macro-fiscal team, the cash management team, and others, (iii) revisiting budget guidelines and address budget comprehensiveness issues, and (iv) continue the development of budget circulars in line with the budget preparation paper and other legal and regulatory changes introduced.

Sub-Component 2.2: Budget Execution (US$ 1.996 million)

22. ***With the support of EFMIS, the MoF started putting in place procedures and take necessary steps toward a more structured budget execution system.*** MoF has: (i) piloted implementation of an action plan in selected line ministries for strengthening treasury management and cash management functions; (ii) drafted a new budget system law and guidelines[40]; (iii) revised the budget classification in line with GFS 2001; (iv) strengthened the institutional capacity in cash management, commitment control, and accounting; (v) undertaken an IT audit of the

[38] This activities aims to outline, among other things, the reporting mechanism within MoF, map the relevant processes, as well answer how and when the budget directorate will interface with its counterparts in line ministries,
[39] i.e., who does what, who can be the core team to interface with, what are their capabilities, etc.
[40] Replacing the outdated 1963 Public Accounting Law.

MoF's information systems and practices; and (vi) developed a PFM reform strategy for 2013-2017.

23. ***Building on EFMIS outputs and through provision of technical assistance, advisory services, mentoring and training and limited IT hardware, FMR 2 plans to support the implementation of the planned budget execution reforms.*** The support will include treasury and cash management, transition to centralized Treasury Single Account operations, enhanced commitment controls and liquidation, and improved accounting practices and reporting based on new budget classification and a new chart of accounts. Activity details are provided below.

24. ***Cash Management: FMR 2 will support continued consolidation of government bank accounts, including closure of inactive accounts and real time access especially to public institutions accounts.*** This will facilitate the transition towards centralized Treasury Single Accounts operations. As consolidation processes improve, the quality and timeliness of cash planning by line ministries will be tackled as to improve the predictability of funding flows. As such, FMR 2 will support the Cash Management Department at MoF to work with staff from 4 large spending ministries on developing their cash plans according to best practices, and monitor the adherence to such plans. In the absence of a voted budget, training will be offered on options to tackle treasury advances and how to integrate in the cash forecasting. On the other hand, cashier operations procedures, of both Local Accounting and Central Accounting and Cashier offices, will also be revisited. The aim will be to reduce cash collection and increase usage of alternate payment mechanism for taxpayers.

25. ***Commitment Controls and Liquidation: FMR 2 will work with MoF to streamline the commitment controls and liquidation processes and revisit the relevant regulations.*** Focus will be given to managing commitments through the implementation of the policy on carry forward of commitments, development of procedures for the treatment of multi-year commitments, improved reporting of commitments, and initiation of commitment ceilings. In addition, procedures to reduce the time of the liquidation process will be implemented. This requires stronger coordination and improvements on the spending procedures of both MoF and line ministries especially to streamline duplication of controls. This will improve the execution of the above cash plans and enhance budget execution processes in general.

26. ***Accounting and Reporting Function: Once approved, the new accounting procedures and budget systems law will introduce significant changes to accounting practices and financial reporting.*** In anticipation, this sub-component will provide technical and advisory assistance along with training and mentoring for MoF staff to implement a new Charts of Accounts (CoA) and Internal Public Sector Accounting Standards (IPSAS) cash basis financial reporting. This requires a series of activities on staffing and capacity improvements and IT systems upgrades. Pre-conditions for IPSAS compliant-reporting are an IT system structured with the specifications to support the new accounting procedures and the implementation of the new Chart of Accounts. FMR 2 will provide further technical support on meeting those conditions.

27. ***The implementation of the above reforms is not possible without a supporting IT system.*** Despite its good technical capacity, the MoF IT unit is currently critically understaffed and faces challenges linked to its hardware, networks and operations.[41] Accordingly, the IT unit is unable to

[41] These challenges are highlighted in detail in the IT audit financed through the EFMIS project.

respond to MoF's increasing requests for automation of data flows and to provide a more functional informatics system that meets the needs of a modern MoF and satisfies the requirements of the changing budget execution processes. Following recommendations of the IT audit, MoF started addressing some of the gaps including initiating (i) the recruitment of 13 new hires in the IT unit to address staffing issue, and (ii) the update of certain licenses for its operating and database systems. FMR 2 will support the efforts to modernize the IT function at MoF to meet the strict and lengthy pre-conditions for a unified GFMIS system.

28. ***A two-tracked approach will be adopted to strengthen the IT system and complement budget execution reforms.*** The first track focuses on stabilizing the existing IT system through (i) providing core COBIT training in IT governance to facilitate better comprehension of the last IT Audit; (ii) hands-on mentoring on the latest hardware and software technologies to develop further institutional capacity; (iii) procuring a basic data warehouse system to improve reporting capabilities and remove risks of corrupting live MoF data; (iv) providing "quick fix" solutions for programing the implementation of IPSAS cash-based accounting standards, BDL transfer data in cash figures to MoF, and other data flow stabilizing applications. The second track provides technical assistance for the production of technical and functional requirements and a complete bidding package for the eventual procurement of a modern integrated GFMIS.

29. ***At the conclusion of FMR 2 - with a successful convergence of the two parallel tracks - an overall assessment of MoF institutional reform progress, capacity development and change management capability will be made.*** This will determine the feasibility of a follow-on GFMIS project using the completed procurement package. If the assessment is not favorable in terms of MoF's readiness to implement a GFMIS, the procurement package can be used, with minor updates, at some time in the future.

Sub-Component 2.3: Public Procurement Reforms (US$ 0.305 million)

30. ***In November 2012, the Council of Ministers endorsed a draft procurement law designating the Central Tender Bureau (CTB) as the central agency managing public procurement.*** Under this law, the CTB moves from its current mandate of focusing on procurement transactions processing, towards a regulatory authority role. The CTB new tasks include (i) proposing public procurement legal and regulatory texts, (ii) prepare standard bidding documents, (iii) train competent personnel for conducting public procurement, (iv) establish and manage a database on all public procurement contract and make the information available to all parties falling under its jurisdiction. Public procurement reforms have positive implications on modernizing and boosting the transparency of budget preparation and execution functions. As such, FMR 2 will support CTB to deliver on the new tasks and envisages the below activities.

31. ***Website Platform for Public Procurement: the sub-component will finance a website developer to design a website platform for public procurement.*** The platform is expected to be very functional and allows for registering contractors and public purchasing agencies, posting advertisement and procurement opportunities, publishing procurement plans and awarded contracts, and report basic statistical information and periodical bulletins submitted to council of ministers and concerned agencies. The platform will also serve as an archive for collected procurement information related to common unit price components and will be populated by standard bidding documents, procurement manuals, and all related regulatory information. The platform is a first and necessary step for e-procurement and is in line with MENA regional

integration efforts on procurement reforms and the use of single entry points for the country public procurement. On the other hand, basic office and IT equipment and furniture for CTB staff will also be provided by the project along with training on operating the platform.

32. ***Revise and Develop sector specific standard bidding documents (SBDs): SBDs in Lebanon are currently not unified across government agencies.*** They are also not comprehensive as they do not cover special procurement of specialized goods, works and services. Despite reform efforts in 2006, the existing standard procurement manuals and bidding documents are not being implemented. Using the leverage of the new law, FMR 2 will support CTB in revising and harmonizing the current SBDs and develop sector-specific bidding documents especially for specialized activities such as extractive industries, energy, pharmaceuticals, or others. The support includes technical assistance and mentoring for devising standards for (i) terms of references, (ii) technical specifications for regular and common services, goods and works, (iii) prequalification standard documents, and (iv) evaluation forms. The assistance will also extend to revise the procurement manual to include comprehensive regulations and guidance for procurement processes.

33. ***Strengthen the CTB and concerned stakeholders capacity: capacity building will be provided to the CTB to fulfill its regulatory and capacity building functions.*** This will include study tours to selected countries with well-established systems and training to CTB staff on regulatory functions, public procurement and procurement audit.

Sub-component 2.4: Internal Audit and Internal Control (US$ 0.352 million)

34. ***The weakness in internal controls and absence of internal audit function in the public sector is a major weakness of the overall PFM system in Lebanon.*** This increases the risks of misuse of public funds. In effect, the 2011 PEFA[42] report continued to rate the internal audit dimension at the lowest possible score. It also pointed out the confusion between the concept of "internal control" and "internal audit", which affected government's perception of the roles of the two functions.

35. ***FMR 2 activities complement the EU twining program and addresses accountability and oversight issues within MoF.*** The objective is to (i) define the requirements of a modern internal control system in compliance with international standards and customized to the Lebanese PFM context, (ii) raise awareness on concepts and practices of such function, (iii) introduce a pilot internal audit function at MOF, and (iv) develop an implementation strategy for the progressive rollout of internal audit throughout line ministries. This is expected to reduce the risks of improper utilization of public funds, fraud, waste and corruption. It is also expected to improve the overall efficiency and effectiveness of the MoF budget operations. Below is a roadmap of activities to be supported by the sub-component.

36. ***Consolidation of diagnostic reviews: FMR 2 will consolidate the existing diagnostic reviews of the internal control framework at MoF.*** This enables the Ministry to identify the respective roles and responsibilities of individual departments and their management in this reform process.

[42] Still to be published.

37. ***Establishing a MoF interdepartmental control and audit work force: upon the issuance of the consolidated review, a workforce will be established and tasked with defining the internal control system and risk management system to be used by all departments within MoF.*** An international expert financed by the project will be engaged to support and mentor the workforce where required. This workforce will also coordinate with relevant stakeholders including the Courts of Accounts, the Central Inspection Board and with other donors notably the EU support for internal controls reforms.

38. ***Piloting an operational Internal Audit function within MoF: Building on the accomplishments of the workforce, a smaller working group will constitute the pilot internal audit function at MOF.*** FMR 2 will provide the required tools for this working group to produce annual audit reports. This pilot function would eventually lay the groundwork for the gradual creation of a decentralized, modern internal audit function in the public sector. It will hence serve as a model for a phased rollout of Internal Audit functions throughout the line ministries in the future.

39. ***Raising awareness, knowledge and training: Extensive training on international standards for internal auditing will be provided for civil servants involved in the workforce on internal control and internal audit.*** In addition, awareness seminars on the relevance of modern internal audit system will be conducted for line management and other concerned staff.

ANNEX 3: IMPLEMENTATION ARRANGEMENTS LEBANON

LEBANON: Fiscal Management Reform Project 2

Project Administration Mechanisms

1. ***Implementation Arrangements. The Ministry of Finance will be the implementation agency of the Project.*** The MoF has been implementing the EFMIS Project (a grant provided by the World Bank to support budget and fiscal reform). The ongoing EFMIS has satisfactory FM rating performance. It is implemented by a PMU within the MoF since the capacity within the Ministry is limited for implementation of World Bank-financed projects. The FMR 2 will also be implemented through a similar type of PMU. For the current project, the MoF has established a PFM Reforms Steering Committee - with members representing all MoF departments – which will act as the technical counterpart and will coordinate activities between the various donors. The members of this committee are senior civil servants. This provides relative stability in that the committee continues to function in the face of political uncertainties and government turnover. The PMU can hence continue to operate despite ministerial changes.

Financial Management

2. ***The following steps are to be taken to mitigate FM-related risks and are set forth in the POM:***

i. A Financial Officer will be recruited to handle the FM aspects of the project. The Financial Officer will be provided with the necessary training by the World Bank on FM reporting requirements and disbursement guidelines.

ii. The current accounting software that is being utilized by EFMIS will be adopted for this project. The software, called “Rockwise”, has been customized to manage World Bank projects and is able to generate the required financial reports as per World Bank reporting requirements.

iii. MoF will update the Project Operational Manual (POM) used by EFMIS, including the FM chapter. The manual will detail the project’s financial management arrangements to be established for carrying out the project FM implementation as well as defining the roles and responsibilities. The updated POM will be finalized within three months after the set-up of the PMU.

iv. The MoF will appoint an acceptable external auditor within six months of project effectiveness as per terms of reference acceptable to the Bank to audit the Project financial statements. The audited annual project financial statements will be publicly disclosed. The audit fees will be covered by the loan funds.

v. MoF through the PMU will prepare on a quarterly basis project interim un-audited reports (IFRs) for submission to the Bank by no later than 45 days at the end of each said quarter.

3. ***Internal Controls.*** ***The MoF has limited written procedures pertaining to FM implementation of donor projects.*** The internal audit function does not yet exist. The Ministry has a controller department that conducts ex-ante reviews on certain transactions. Similarly, the expenditures department performs some verification on certain expenditures while the Court of Accounts (CoA) performs ex-ante review based on predefined thresholds and the nature of expenditures. For the purpose of the project, the MoF will prepare and update a financial management chapter as part of the project operational manual which will include detailed description of project's accounting and financial management procedures related to the Project FM implementation. The POM will be reviewed and cleared by the World Bank.

4. ***Financial Reporting.*** ***The project will be required to issue quarterly Interim unaudited Financial Reports (IFRs) and annual Project Financial Statements (PFS) for submission to the Bank.*** These will have the following specificities:

i. *Quarterly IFRs:* The Project's IFRs, prepared in accordance with International Public Sector Accounting Standards (IPSAS) – cash basis and generated from the project accounting software, will be sent to the Bank by no later than 45 days after the end of each quarter. The format and content of IFRs will be included in the POM. The Project IFRs will be composed of:
   a. Statement of Cash Receipts and Payments by category for the year then ending and cumulatively from inception date up till the year ending.
   b. Accounting policies and explanatory notes including a footnote disclosure on schedules:
      - Statement of Designated Account reconciling period-opening and end balances;
      - Statement of project commitments, showing contract amounts committed, paid, and unpaid under each project's signed contract;
      - Detailed expenditures by components and by category in addition to a fixed assets list.

ii. *Project Financial Statements (PFS):* The PFSs, prepared in accordance with IPSAS – bash basis - should contain the same information as the quarterly IFRs but cover an annual period. The audited PFS would be submitted to the Bank no later than six months after the end of each fiscal year[43] (see External Audit Arrangements below).

Disbursements

5. ***Designated Account: To ensure that funds are readily available for the project implementation, MoF will open and operate a Designated Account (DA) in US dollars at the BDL, and MoF through the PMU will maintain this Designated Account.*** Deposits into, and payments from the DA will be made in accordance with the provisions which is stated in the project's Loan Agreement and in accordance with World Bank Disbursement Guidelines. Eligible expenditures will be financed out the Loan proceeds including Goods, Non-Consulting Services, Consultants 'services, Incremental Operating Costs, Training, Workshops and Study Tours. The Ceiling of the DA would be US$600,000. The MoF, through the PMU, will be responsible for submitting replenishment applications with appropriate supporting documentation. Authorized signatories, names, and corresponding specimens of their signature will be submitted to the Bank prior to the receipt of the first Withdrawal Application.

[43] Project fiscal year ends December 31.

6. ***Disbursement and Flow of Funds: The proceeds of the Loan would be disbursed in accordance with the traditional disbursement procedures of the Bank and will be used to finance project activities through the disbursement procedures currently used: i.e.*** Advances, Reimbursement/Replenishment and Special Commitment. Replenishment and Reimbursement Withdrawal Applications will be accompanied by Statement of Expenditures (SOEs) in accordance with the procedures described in the Disbursement Letter and the Bank's "Disbursement Guidelines". Interim Unaudited Financial Reports and Annual Financial Statements will be used as a financial reporting mechanism and not for disbursement purposes. The minimum application size for reimbursement will be the equivalent of 20 percent of the Advance ceiling amount. The Bank will honor eligible expenditures completed, services rendered and goods delivered by the project closing date. A four-month grace period will be granted to allow for the payment of any eligible expenditures incurred (i.e. services, goods or works, received and accepted) before the Loan Closing Date.

7. ***Statement of Expenditures: All Reimbursement and Designated Account Replenishment Applications for withdrawal of proceeds from the loan account will be fully documented, while (a) expenditures under contracts with an estimated value of US$100,000 or less for Goods and Consulting Firms; and (b) US$50,000 or less for Individual Consultants, Incremental Operating Costs, Training, Workshops and Study Tours will be claimed on the basis of SOEs.*** The documentation supporting expenditures will be retained at Project Implementation Unit and will be readily accessible for review by the external auditors and periodic Bank supervision missions.

8. ***Advances will be channeled through the Treasury Single Account at MoF (segregated transit sub-account under the account 36 that is used to account for all donors in flow funds) and deposited into the project's DA at BDL in US dollars.***

9. ***e-Disbursement: The World Bank has introduced the e-disbursement for all Lebanon supported projects.*** Under e-disbursement, all transactions will be conducted and associated supporting documents scanned and transmitted on line through the Bank's Client Connection system. E-disbursement will considerably speed up disbursements and facilitate project implementation. It is for mandatory application for all World Bank-financed projects starting January, 2013.

10. ***The following table specifies the categories of eligible expenditures that will be financed out of the proceeds of the IBRD Loan:***

Category	Amount of the Loan Allocated (expressed in USD)	Percentage of Expenditures to be financed (inclusive of Taxes)
(1) Goods, non-consulting services, consultants' services, Incremental Operating Costs, Training, Workshops and Study Tours	5,187,000	100%
(2) Front-end Fee	13,000	Amount payable pursuant to Section 2.03 of this Agreement in accordance with Section 2.07 (b) of the General Conditions
(3) Interest Rate Cap or Interest Rate Collar premium	0	Amount due pursuant to Section 2.07(c) of this Agreement
TOTAL AMOUNT	5,200,000	

11. ***No withdrawal shall be made for payments made prior to the date of the Loan Agreement, except that withdrawals up to an aggregate amount not to exceed US$1,040,000 equivalent may be made for payments made prior to this date but on or after September 15, 2013, for Eligible Expenditures under Category 1.***

12. ***Authorized Signatories:*** Authorized signatories will be nominated by MoF to sign the Withdrawal Applications (WAs). Names and corresponding specimen of their signatures will be submitted to the Bank prior to the receipt of the first WA (advance to DA). Each WA will be approved and signed by the authorized signatories.

13. ***Governance and Anti-Corruption (GAC).*** Fraud and corruption may affect the Project resources, thus negatively impacting the Project outcomes. The World Bank worked closely with the client to develop an integrated understanding of possible vulnerabilities and agreed on actions to mitigate the risks. The proposed fiduciary arrangements, including POM with a detailed FM chapter, financial reporting requirements and external audit are expected to address the risk of fraud and corruption.

Controls and Audits

14. ***External Audit arrangements:*** The PFS will be audited by an independent private external auditor acceptable to the World Bank. The audit will be comprehensive and will cover all aspects of the project, including compliance with the POM, review of effectiveness of the internal controls system, and compliance with the Financing Agreement. The audit will be carried out in accordance with International Standards on Auditing. The audit report and PFSs, along with management letter, will be submitted to Bank no later than six months after the end of each fiscal year. In addition, the project management letter will contain the external auditor assessment of the internal controls, accounting system, and compliance with financial covenants in the Loan Agreement. The audit TORs was finalized and agreed upon with the Bank during negotiations. The external auditor is expected to be engaged within six months of project effectiveness.

15. ***Moreover, according to the Bank's disclosure policy, the Bank makes publicly available the borrowers' audited annual financial statements for all investment projects as per OP/BP 10.00.*** Accordingly, this Project's audited annual financial statements will be made available to the public.

16. ***Supporting Documentation and Record Keeping. All supporting documentation was obtained to support the conclusions recorded in the FMAR.***

Procurement

Procurement Capacity Assessment

17. ***Implementing agency: The MoF abides by the Procurement Law No. 14969 dated December 30, 1963.*** The Ministry operates under the ceiling of LBP 100 Million (US$67,000 equivalent). Above that ceiling, bidding is processed centrally by the central tender board.

18. ***Past experience in World-Bank projects: The MoF has outsourced qualified procurement staff and successfully implemented the first EFMIS project.*** Procurement was processed successfully following the Bank's guidelines, using consultancy selection methods and shopping. Procurement post reviews exercises have proven diligent procurement processing and contract management and were satisfactorily rated. The EFMIS project developed an operational manual, an updated version of which willbe used in the second project.

19. ***Applied taxes:*** The following are the three types of taxes applied: (i) Stamp Duties of (a) 3 per thousand of the contract price for contract registration at Ministry of Finance (MOF), and (b) 3 per thousand on each payment; (ii) Value Added Taxes (VAT) of 10 percent applied on consultants and contractors who are registered and eligible for VAT; and (iii) Income Taxes that are a flat rate of 7.5 percent for non-registered consultants (TIN number) and variable for registered consultants, depending on their job classification at MoF. Exemption of consultants from Income Taxes may be observed if they are registered in countries that have entered with Lebanon into agreements prohibiting double taxation. Contracts financed by international donor proceeds are exempted from VAT (Law No 379 dated December 14, 2001).

20. ***Audit: Currently the Ministry does not have an internal audit system but relies on the Court of Accounts for ex-ante and ex-post reviews.*** The Central Inspection plays a role in procurement verifications and in complaints cases.

21. ***Current Procurement Staff:*** The Ministry procurement department is composed of the head of department (17-year experience) and three staff (Bachelor degree with an average of 2 to 5 years of experience). In addition to procurement and human resources departments, the MoF comprise a special IT department in which the procurement thresholds are waived.

22. ***Procurement Planning: The activities are planned according to availability of budget released in March of the given year.*** The planning is thus done ad-hoc; no particular attention is given to packaging activities. The department keeps track of prices and market offered items.

23. ***The overall procurement implementation risk is assessed as Substantial.***

Proposed Procurement Arrangements

24. ***Project guidelines:*** World Bank "Guidelines on Preventing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants" dated October 15, 2006 and updated January 2011, "Guidelines: Procurement of Goods, Works and Non- consulting Services under IBRD Loans and IDA Credits and Grants by World Bank Borrowers" dated January 2011 and "Guidelines: Selection and Employment of Consultants under IBRD Loans and IDA Credits and Grants by World Bank Borrowers" dated January 2011 shall apply.

25. ***Procurement methods for goods and non-consulting service:*** the project is expected to conduct (i) international competitive bidding (ICB); (ii) national competitive bidding (NCB) for which shall be used either ICB -or a translated version- or develop Standard Bidding Documents acceptable to the Bank as mentioned in clauses 3.3 and 3.4 of the procurement guidelines, (iii) shopping, (iv) framework agreements, and (v) direct contracting.

26. ***Selection of Consultants:*** the project is expected to conduct (i) Quality and Cost Based Selections (QCBS), (ii) Selection under a Fixed Budget (FBS), (iii) Least-Cost Selection (LCS), (iv) Selection Based on the Consultants' Qualifications (CQS), (v) Single Source Selection (SSS), and (vi) Selection of Individual Consultants including sole sourcing procedures. In view that the first project (EFMIS) design was found satisfactory, it is anticipated that FMR 2 may retain individual consultants already identified competitively.

27. ***Staff:*** The procurement function shall be supported by the Ministry's technical staff but there will be need for outsourcing a Procurement Officer.

28. ***Project Operation Manual (POM):*** The manual used in EFMIS is proposed to be updated and used for the project. The procurement section in the manual shall specify the procurement processing and contract management. It shall comprise the NCB as approved by the Bank and will also tackle the record-keeping requirements and the complaint mechanism expected arrangements.

29. ***Procurement plan:*** An initial procurement plan, dated July 15, 2013, for the life of the project has been developed by the Ministry. It defines the prior review and procurement methods thresholds. It will be updated by MoF and reviewed by the Bank at least twice a year or as seen necessary. The following is a snapshot of the procurement plan:

Consultancy for major Assignments with Selection Methods and Time Schedule

Proc. System Ref. #	Comp	Sub-Comp	Location/ Description of Assignment	Estimated Cost (US$)	Selection Method	Bank Rev.	Expected contract date
FC001	C2	2.2	Development of GFMIS technical specifications, requirements, complete bidding package	250,000	QCBS	PO	Jul-14
FC002	C2	2.3	Revision of SBD and procurement manual; Development of standards and forms (SBD, specifications, TOR); Development of regular sepcifcations;	160,000	QCBS	PO	Jun-14
FC003	C2	2.4	Review and mapping of existing diagnostic reviews and description of roles and responsibilities & Strengthening internal control - interdepartmental internal control work force & Introduce a pilot internal audit function & trg	176,187	QCBS	PO	Jul-14
FC004	C3	3.1	Independent Audit of the project	20,000	LCS	PR	Jun-14
IC	All	All	Individual consultants	3,400,000	IC	PO/PR	

Procurement of major Goods with Procurement Methods and Time Schedule

Proc. System Ref. #	Comp	Sub-Comp	Location/ Description of Assignment	Estimated Cost (US$)	Selection Method	Bank Rev.	Expected contract date
PG001	C2	2.2	Data warehouse minimum configuration w/o operating system or database software	500,000	ICB	PR	29-Apr

30. ***The frequency of supervision missions and post procurement reviews will be twice a year and once a year, respectively.*** In post procurement review, a sample of 15% of contracts eligible for post review shall be covered.

31. ***Mitigation measures:*** The following measures are proposed to mitigate the risk rating to Moderate: (i) include in the ToRs of the project's audit a review on the time taken to provide procurement decisions and justifications when those decisions are over-rided; (ii) agree on a training program to be implemented during the project; (iii) provide appropriate support (staff, training, tools) to prepare a detailed procurement plan with clear linkages to the project development objectives; (iv) prepare acceptable sample bidding documents for National Competitive Bidding; (v) ensure clear and quantifiable evaluation criteria and monitor compliance; (vi) set deadlines for complaints submission and for decision making by the MOF; (vii) establish a system to monitor and expedite contract modifications or change orders and include this requirement as part of the TOR for procurement audits; (viii) agree on appropriate publication (i.e. on a website or press bulletins) of procurement decisions.

Environmental and Social (including safeguards)

32. ***FMR 2 is classified as a "Category C" project and does not trigger any environmental or social safeguards.*** FMR 2 project aims to build fiscal policy analysis capacity, improve the budgetary allocation of public resources, enhance the efficiency and transparency of the government financial management systems, and tighten the control environment for more effective use of public resources. As such, the Project finances capacity building, technical assistance, training, and advisory services for Ministry of Finance and other government stakeholders. These activities do not include any physical infrastructure. No new buildings are to be constructed. Only some potential limited upgrades of existing computer rooms might be required before installing some of the IT systems or equipment supported through project. Therefore, this is not expected to have any environmental impact. Additionally, the Project does not focus on any particular population group or social programs, and does not call for any resettlement.

Monitoring & Evaluation

33. ***The PMU will be responsible for the daily project implementation.*** The PMU will prepare quarterly progress reports, including updates on the indicators identified in the results framework (Annex 1).

ANNEX 4: OPERATIONAL RISK ASSESSMENT FRAMEWORK (ORAF)

LEBANON: Lebanon Fiscal Management Reform Project 2

<table>
<tr><td colspan="13">Project Stakeholder Risks</td></tr>
<tr><td>Stakeholder Risk</td><td colspan="2">Rating</td><td colspan="10">Moderate</td></tr>
<tr><td rowspan="6">Risk Description:

The Central Bank (BDL), the Courts of Accounts (CoA), and Parliamentary Budget Committee might oppose some of the proposed reform measures that can overlap or alter their responsibilities. This is particularly true in the area of debt management and operations for BDL, internal controls and auditing for CoA, and the new budget law that replaces the 1963 Public Accounting Law. Also government support for PFM reforms might shift following the upcoming Parliamentary elections and the subsequent change in cabinet.</td><td colspan="12">Risk Management:</td></tr>
<tr><td colspan="12">Joint committees and workforces have been created between MoF and various stakeholders. These are currently operational and meet on regular basis. Among such form of collaboration is:

a) The high debt committee includes senior management from MoF and BDL and discusses all issues related to debt management. Technical teams from both institutions collaborate on regular basis in preparation for these meetings.

b) The joint workforce between MoF and CoA that deals with audit and controls issues including discussions over public accounts.

c) The consultation process that MoF put in place during the preparation of the draft budget systems law and which included CoA and the Budget committee at Parliament. These consultations focused on the reforms to the Public Accounting Law.</td></tr>
<tr><td>Resp:</td><td>Client</td><td>Status:</td><td>Completed</td><td>Stage:</td><td>Preparation</td><td>Recurrent:</td><td></td><td>Due Date:</td><td>04-Oct-2013</td><td>Frequency:</td><td></td></tr>
<tr><td colspan="12">Risk Management:</td></tr>
<tr><td colspan="12">The Bank is engaged through the current EFMIS with all the above stakeholders, in addition to the PM office, in discussions over the reforms in the different PFM areas (Macro fiscal, budget preparation, budget execution, procurement and control environment). Additionally, the Bank has consulted with representatives from these different agencies on the design of the new project. Such consultation process will continue throughout implementation through the daily interactions of the PMU on project activities and through direct discussions during World Bank supervision missions. Importantly, the Bank regularly engages with senior MoF leadership (on both management and technical levels), which has demonstrated a commitment to the program, further evidenced by the loan instrument.</td></tr>
<tr><td>Resp:</td><td>Bank</td><td>Status:</td><td>In Progress</td><td>Stage:</td><td>Both</td><td>Recurrent:</td><td>☑</td><td>Due Date:</td><td></td><td>Frequency:</td><td>Continuous</td></tr>
</table>

	Risk Management: MoF has adopted a PFM reform plan with a detailed road-map for implementation over the medium term. This implementation will be overseen by a newly created Budget Reforms Steering Committee composed of senior civil service officials representing all MoF budget functions. The medium-term focus of the action plan with its defined activities, and the permanent nature of the implementing committee increases reform ownership and insulates PFM reforms to a certain extent from the fluctuation arising from changing governments or changes in the political environment.
	Resp: Client | Status: Completed | Stage: Preparation | Recurrent: ☑ | Due Date: | Frequency: Yearly

Implementing Agency (IA) Risks (including Fiduciary Risks)

Capacity	Rating: Substantial
Risk Description: The Ministry of Finance is the implementing agency of this project. It has built capacity in such type of operation in the last four years by executing the EFMIS project. However risks can be identified: On Staffing: staffing gaps could constitute an important risk for the execution of the proposed activities. In effect, the stringent civil service board regulations are a major bottleneck for recruiting staff with the required education and professional qualification to fulfill reforms under the various components of the project. This is the case as terms of references and remunerations are not aligned with the modern functions of a ministry of finance. This often leaves the Ministry with severe lack of staff in certain key departments notably the IT, the	**Risk Management:** MoF is currently working with the civil service bureau on changing some of the hiring requirements especially in terms of changing the ToRs of jobs posted, changing the entry exams content to tailor the need of the new positions, and introduce a new interviews stage. Resp: Client | Status: In Progress | Stage: Both | Recurrent: ☑ | Due Date: | Frequency: Continuous **Risk Management:** The Bank will help the Ministry design ToRs for the key empty positions under the different sub-components of the project. This will be part of the restructuring efforts supported by the project notably in the budget department, the macro-fiscal unit, the public debt department and within some treasury at MoF. FMR 2 will also be providing on the job training as part of the capacity building efforts. Indeed, the engagement will be under the form of an incubation-type model in which international and national experts will work directly with civil servants and provide hands-on training in order to design solutions and implement the identified reforms. Resp: Bank | Status: In Progress | Stage: Both | Recurrent: ☑ | Due Date: | Frequency: Continuous **Risk Management:** With support from the project, the MoF will continue working on the formal PFM training strategy first initiated under

<table>
<tr><td rowspan="6">macro-fiscal unit, the budget department, treasury, and the public debt department.

On project fiduciary: the lack of project fiduciary staff at MoF could result in improper implementation of procurement activities, delays in decision-making on procurement processing, and unsatisfactory financial reporting.

On Procurement : (i) Obsolescence in procurement and contract management knowledge leading to continued poor quality of results; (ii) Delay to project processing and implementation due to lack of proper planning, (iii) Implementation delays because no standardized Bidding Documents for NCB, known to local bidders, (iv) Lack of public oversight may lead to abuse and corruption.</td><td colspan="6">EFMIS. Implementation plans for the strategy will be identified as to institutionalize the training process within MoF.</td></tr>
<tr><td>Resp: Client</td><td>Status: Not Yet Due</td><td>Stage: Implementation</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Continuous</td></tr>
<tr><td colspan="6">Risk Management:

Procurement: (i) Include review of time taken to make decisions and justifications for over-riding decisions in the TOR of audits, (ii) Agree on a training program (internal/ external), (iii) Arrange for appropriate support (staff, training, tools), (iv) Prepare sample bidding documents for National Competitive Bidding, (v) Set deadlines for submission of complaints and for decision making by the agency, (vi) Establish system to monitor and expedite contract modifications. Include this requirement as part of the TOR for procurement audits, (vii) Agree on appropriate publication (i.e. on a website or press bulletins) of procurement decisions and other relevant information as minimum.</td></tr>
<tr><td>Resp: Both</td><td>Status: Not Yet Due</td><td>Stage: Implementation</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Yearly</td></tr>
<tr><td colspan="6">Risk Management:

The project will establish a PMU (including a Financial Officer, and an Accountant) and provide additional resources to supplement the existing fiduciary capacity of the MOF.</td></tr>
<tr><td>Resp: Client</td><td>Status: Not Yet Due</td><td>Stage: Implementation</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Continuous</td></tr>
<tr><td>Governance</td><td>Rating</td><td colspan="5">Substantial</td></tr>
<tr><td>Risk Description:

MoF lacks an external audit function as it is subject to the Court of Accounts ex post review. The latter experiences lack of quality and timely reports in many instances. Also the</td><td colspan="6">Risk Management:

One of the project's sub-component is designed to raise awareness of control and audits in the public sector; streamline and strengthen the internal control environment and procedures at MOF; and establish an internal audit function in compliance with international standards. The expected outcome is increased accountability and transparency of MOF operations, enhanced risk management, and availability of an independent and objective assurance of the efficiency and effectiveness of its internal controls.</td></tr>
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<table>
<tr><td rowspan="4">control environment within the Ministry remains weak. The Ministry has a limited internal audit system that is not operating at internationally accepted standards, nor does it have an internal control function.</td><td>Resp: Bank</td><td>Status: Not Yet Due</td><td>Stage: Implementation</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Yearly</td></tr>
<tr><td colspan="6">Risk Management:

For the purpose of the project, the MoF will get into a contract with an independent external auditor. The auditor will audit the project financial statements and will submit and audit report and management letter within six (6) months after the end of each fiscal year</td></tr>
<tr><td>Resp: Client</td><td>Status: Not Yet Due</td><td>Stage: Implementation</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Yearly</td></tr>
<tr><td colspan="6"></td></tr>
<tr><td colspan="7">Project Risks</td></tr>
<tr><td>Design</td><td>Rating</td><td colspan="5">Moderate</td></tr>
<tr><td rowspan="4">Risk Description:

The design risks are identified as the following:

(i) The large scope of the project and MoF's limited absorptive capacity to implement all the activities under the five sub-components.

(ii) The need for quick executive decisions from MoF senior management and its commitment in pushing for cabinet approvals of certain regulations and legislation to implement to proposed structural reforms under this project.

(iii) The lack of strong communication across MoF departments especially that project activities will often need to be implemented by working groups from across the various functions of the Ministry. This communication becomes weaker when external stakeholders are</td><td colspan="6">Risk Management:

The design of FMR 2 incorporates some of the lessons learned in the EFMIS project especially as many activities are considered as a continuation of the previous efforts. These design features for FMR 2 are:

(i) The sequencing of activities to tackle the limitations in the absorptive capacity of MoF and therefore improve implementation. The inception reports prepared for each sub-component (or areas of engagement) will include a clear execution map with the appropriate sequencing of deliverables.

(ii) An opportunistic approach for reforms where activities are pushed more aggressively for sub-components where favorable political environment are in-place.

(iii) Adopt an incubation-type model in which international and local experts work jointly with MoF working groups to design solutions and implement changes. This comes with hands-on and on-the-job training to provide capacity building for civil servants staff especially in areas where mismatches in personnel skills and academic background are identified.</td></tr>
<tr><td>Resp: Bank</td><td>Status: In Progress</td><td>Stage: Preparation</td><td>Recurrent:</td><td>Due Date: 31-Oct-2014</td><td>Frequency:</td></tr>
<tr><td colspan="6">Risk Management:</td></tr>
<tr><td colspan="6">Capacity building will be provided under the various sub-components of the project by international and local experts.</td></tr>
</table>

<table>
<tr><td rowspan="2">involved.

(iv) Weak staffing capacity and regulatory barriers to hire personnel with specialized skills risks delaying the planned deliverables especially those that introduce new functions into the ministry.</td><td colspan="6">Additionally training manuals will be designed at the ministry to ensure the institutionalization of the capacity building process, and targeted workshops will be held.</td></tr>
<tr><td>Resp: Bank</td><td>Status: Not Yet Due</td><td>Stage: Implementation</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Yearly</td></tr>
<tr><td>Social and Environmental</td><td colspan="6">Rating Low</td></tr>
<tr><td rowspan="2">Risk Description:

The project is a "category C" and does not trigger any environmental or social safeguards. The project finances capacity building activities and technical assistance in the areas of fiscal policy, debt management and budget processes. These have no social or environmental implications.</td><td colspan="6">Risk Management:</td></tr>
<tr><td>Resp:</td><td>Status:</td><td>Stage:</td><td>Recurrent:</td><td>Due Date:</td><td>Frequency:</td></tr>
<tr><td>Program and Donor</td><td colspan="6">Rating Moderate</td></tr>
<tr><td rowspan="4">Risk Description:

Donor-supported PFM reform projects are numerous and include programs supported by the UNDP, The World Bank, the EU, and the IMF-METAC. The fragmentation of these programs, their large operational scopes, and the weak institutional capacity at MoF for donor coordination increases the risk of overlap and therefore inefficient use of support resources.</td><td colspan="6">Risk Management:

The PFM reform strategy, formulated and adopted by MoF, serves as the guiding document for donor supported reforms as it outlines the Ministry's needs, objectives and agenda over the medium-term.</td></tr>
<tr><td>Resp: Client</td><td>Status: In Progress</td><td>Stage: Both</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Continuous</td></tr>
<tr><td colspan="6">Risk Management:

The MoF has created a PFM reforms steering committee to implement its PFM strategy. The committee, which represents senior officials from all departments within the Ministry, will be tasked with coordinating the various donor funded projects. Indeed, the committee will assume the role of the technical counterpart that will be overseeing the Donor activities and will evaluate their relevance within the outlined strategy.</td></tr>
<tr><td>Resp: Client</td><td>Status: In</td><td>Stage: Implementatio</td><td>Recurrent: ☑</td><td>Due</td><td>Frequency: Continuous</td></tr>
</table>

<table>
<tr><td rowspan="3"></td><td></td><td>Progress</td><td>n</td><td></td><td>Date:</td><td></td></tr>
<tr><td colspan="6">Risk Management:

During preparation: The World Bank team has consulted extensively with key stakeholders and Donors on the design of FMR 2 and its areas of support. This is particularly the case with the comprehensive EU twinning project. The design of the two projects allows for synergies especially that the EU twinning arrangement looks at overall frameworks using short missions, while FMR 2 focuses further on implementation using incubator-type approach. FMR 2 will implement relevant findings from the EU project. This is most visible in the internal audit and internal controls sub-component.

During implementation: the PMU will play an active role in updating donors on FMR 2 activities. It will share information on the content and timing of these activities and will work closely with the government counterparts to avoid overlap. The physical location of the PMU, within the premise of MoF, enables it to conduct such interaction on a daily or frequent basis. Furthermore, the Bank will consult with engaged donors during supervision missions and other points, as needed.</td></tr>
<tr><td>Resp: Bank</td><td>Status: In Progress</td><td>Stage: Both</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Quarterly</td></tr>
<tr><td>Delivery Monitoring and Sustainability</td><td>Rating</td><td colspan="5">Substantial</td></tr>
<tr><td rowspan="4">Risk Description:

Monitoring and Evaluation capacity in Lebanon is weak and no country system is currently in place to monitor PFM reforms. Also sustainability risks continue to be substantial as (i) several practices and procedures remain not documented; and (ii) many civil servants engaged in the implementation of the core project's activities lack job security as they are under daily or hourly contractual basis.</td><td colspan="6">Risk Management:

FMR 2 plans to continue with the work currently undertaken under EFMIS and document existing procedures especially in budget execution (cash management, accounting, commitment controls, IT systems, etc...). Manuals will therefore be produced. This allows the project to institutionalize reforms, increase transparency of operations, and have clear guidelines to avoid mismanagement.</td></tr>
<tr><td>Resp: Client</td><td>Status: In Progress</td><td>Stage: Both</td><td>Recurrent: ☑</td><td>Due Date:</td><td>Frequency: Yearly</td></tr>
<tr><td colspan="6">Risk Management:

The MoF is actively working with the civil service bureau to solve the recruitment issues with the objective of accelerating the hiring process and fill vacancies with civil servants with open ended contracts.</td></tr>
<tr><td>Resp: Client</td><td>Status: In Progress</td><td>Stage: Both</td><td>Recurrent:</td><td>Due Date: 30-Jun-2014</td><td>Frequency:</td></tr>
</table>

	Risk Management: The FMR 2 project will finance IT warehouse and other IT fixes that will improve significantly the reporting functions of the Ministry. This is expected to improve the quality and quantity of data/information collected along with the reporting capabilities of the Ministry. This will in turn allow for a notable improvement in the monitoring and evaluation system.

Resp:	Bank	Status:	Not Yet Due	Stage:	Implementation	Recurrent:	Due Date:	30-Jun-2014	Frequency:

6. Overall Risk

Overall Implementation Risk:

Substantial

Risk Description:

1) Institutional Risk: increased country risks and political uncertainty accentuated by the ramifications of the Syrian crisis and the deadlock over Parliamentary elections which delays executive and regulatory decisions needed to push PFM reforms forward.One of the most significant examples is the delay in the approval of a budget. At this stage of reforms quick fixes are being exacerbated quickly, structural measures will need to be addressed to ensure the achievement of the project's objectives. Also, from past experience in EFMIS, political volatility in Lebanon will certainly influence the pace of reforms especially in times of changing governments.

2) Absorptive Capacity and Staffing Limitations: The limited absorptive capacity at the Ministry of Finance, line ministries and other stakeholders in the current staffing context where filling increasing job vacancies and mobilizing human resources is proving to be a difficult and slow task. Regulatory, administrative and political barriers are all contributing to this problem. Without staffing in crucial areas, for example IT department, the risks of not implementing certain activities supported under FMR 2 is substantial.

3) Weak Donor Coordination: weak donor coordination could lead tp potential overlap in activities and competition over deliverables. This would potentially lead to client fatigue, weaken FMR 2 implementation, and therefore impact the achievement of the project's development objectives. For this purpose, the PMU will play an important role in the daily interaction with the different stakeholders including donors, and the World Bank team will support these interactions through its supervision role.

ANNEX 5: IMPLEMENTATION SUPPORT PLAN

LEBANON: Second Fiscal Management Reform Project

1. ***The strategy for implementation support has been developed based on the nature of the project and its risk profile.*** It aims at making the implementation support to the client more flexible an efficient, and will focus on implementation of the risk mitigation measures defined in the Operational Risk Assessment Framework.

2. ***FMR 2 builds on the modalities of engagement outlined in the EFMIS project.*** The project finances consultants to provide technical assistance and training for civil servants on the identified reform components. It also finances IT equipment and software to improve budgetary processes. The PMU will coordinate these activities in collaboration with the MoF PFM reform steering committee. While the latter acts as the technical counterpart, the Minister and Director General of MoF play a strategic guidance role and will be informed of progress under the project on a regular basis and consulted as needed.

3. ***The design and implementation of FMR 2 incorporates the lessons learned from EFMIS namely in strengthening activity sequencing efforts, providing flexibility in pushing for deliverables, and adopting an incubation-type approach during implementation.*** First, the sequencing of activities allows for the tackling of the limitations imposed by the absorptive capacity of MoF. Therefore, the inception reports prepared for various areas of engagement are expected to include a clear execution map with the appropriate sequencing of deliverables. Second, a flexible approach for reforms will be adopted to reduce the impact of political volatility in the country. During favorable political environment, activities will be pushed more strongly. Third, FMR 2 adopts an incubation-type model in which international and local experts work jointly with MoF working groups to design solutions and implement changes. This is accompanied by hands-on and on-the-job training. The objective is to provide capacity building for civil servants especially in areas where mismatches in personnel skills and academic background are identified.

Implementation Support Plan

4. ***The World Bank team, located in part in Beirut, will follow-up on implementation matters regularly as part of the ongoing dialogue with the MoF.*** The World Bank team consists of specialists in the areas of PFM, Macro-Fiscal Policy, Debt Management, IT, Procurement and Financial Management. It will be supported by the resident Lead Country Economist for the policy dialogue aspects. Full implementation support missions, including on financial management aspects, are expected to be carried out on semi-annual basis.

Skills Mix Required

Skills Required	Number of Staff Weeks (estimated)	Number of Trips	Comments
TTL	30	Approx. 4 per year	Implementation support, policy dialogue, project and client management, and communication
Public Sector Spec.	24	Field-based	Implementation support and

			policy dialogue
IFMIS Expert	24	Approx. 2 per year	Implementation support, policy dialogue and on-the-job support
Procurement Spec.	12	Field-based	Procurement implementation support
FM Specialist	9	Field-based	FM implementation support, and audit
Team Assistant	9	Field based	Correspondence, filing, and mission planning
M&E Specialist	3	1	

5. ***The World Bank team members are based in Beirut, Washington D.C, and in the MENA region and will be available to provide timely, efficient, and effective implementation support to the client. Detailed inputs from the Bank team are outlined below:***

- *Technical inputs.* The World Bank will provide implementation support. The Bank team specialists will monitor the project's deliverables, provide no-objection on the various activities, and engage with MoF's senior management, technical staff, PMU and hired experts; to advise on the direction and priorities of the reforms. This technical support will be conducted on continuous basis and as needed.

- *Procurement, financial management and disbursement requirements and input.* Training to PMU members and other concerned Ministry staff will be provided as needed by the procurement and financial management specialists of the team. The Bank specialists are based in the Bank's Lebanon Country Office and hence can be mobilized quickly. In addition to the formal semi-annual implementation support missions, procurement and FM specific supervision and follow-up will be carried out on a timely basis. Additionally, the activities outlined under the project sub-components 2.3 (Procurement reforms) and 2.4 (Internal controls and internal audit) are tailored with the objective of improving the efficiency of both procurement and financial management within government, and institutionalize the capacity building process within those fields.

- *Operation.* The Task Team Leader, with the help of the Task Team members, will provide timely and close supervision of all operational aspects, as well as coordination with the client, beneficiaries, stakeholders, and among team members. If needed, the PMU's project manager will assist especially on the day-to-day follow-up with client and stakeholders.

- *Donor coordination.* The World Bank team and the PMU will play an active role in sharing updates with donors on activities to be performed under the project. Timely meetings with the representatives of various donor groups will be conducted to ensure that the complementarity between activities is sustained. The MoF senior management and the Budget Reform Steering Committee will take the lead in donor coordination lead to strengthen synergies between projects and ensure donor support alignment with the PFM reform strategy.