PUBLIC
SIMULTANEOUS DISCLOSURE

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

ECUADOR

STATE-OWNED ENTERPRISE REFORM SUPPORT PROGRAM

(EC-L1251)

LOAN PROPOSAL

This document was prepared by the project team consisting of: Juan Luis Gómez (FMM/CEC), Project Team Leader; Emilio Pineda (FMM/CAR), Alternate Project Team Leader; Carlos Echeverría (ENE/CEC); Pilar Jiménez de Arechaga (LEG/SGO); Mariela Sánchez and Alexandra Sánchez (CAN/CEC); Juan Carlos Dugand and Carolina Escudero (FMP/CEC); and Ida M. Fernández Paino, Diana Champi, and Ana Calvo (IFD/FMM).

CONTENTS

ANNEXES	
Annex I	Summary Development Effectiveness Matrix (DEM)
Annex II	Results Matrix
Annex III	Fiduciary Agreements and Requirements

REQUIRED LINKS
1. Multiyear execution plan and annual work plan
2. Monitoring and evaluation plan
3. Procurement Plan

OPTIONAL LINKS
1. Safeguard policy filter and safeguard screening form
2. Project economic analysis
3. Itemized budget
4. Draft Program Operating Regulations

ABBREVIATIONS

BCE	Banco Central del Ecuador [Central Bank of Ecuador]
CELEC	Corporación Eléctrica del Ecuador
CGE	Contraloría General del Estado [Office of the Comptroller General]
CNEL	Corporación Nacional de Electricidad
CUT	Cuenta Única de Tesorería [Treasury Single Account]
DNEP	Dirección Nacional de Empresas Públicas [National State-owned Enterprise Directorate]
e-SIGEF	Sistema integrada de gestión financiera [Integrated financial management system]
EMCO	Empresa Coordinadora de las Empresas Públicas [State-owned Enterprise Holding Company]
ICB	International competitive bidding
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
LOEP	Ley Orgánica Empresas Públicas [State-owned Enterprises Act]
LOSEP	Ley Orgánica de Servicio Público [Public Service Act]
LSS	Ley de la Seguridad Social [Social Security Act]
MEF	Ministry of Economy and Finance
MERNNR	Ministry of Energy and Nonrenewable Natural Resources
MTOP	Ministry of Transportation and Public Works
NCB	National competitive bidding
NFPS	Nonfinancial public sector
OECD	Organisation for Economic Co-operation and Development
PAM	Petroamazonas
PBL	Policy-based loan
PEC	Petroecuador
PGE	Presupuesto General del Estado [General State Budget]
SERCOP	Servicio Nacional de Contratación Pública [National Public Procurement Service]
SNCP	Sistema Nacional de Contratación Pública [National Public Procurement System]
SOE	State-owned enterprise
SRI	Servicio de Rentas Internas [Internal Revenue Service]
TAME	Ecuadorian National Airline

PROJECT SUMMARY
ECUADOR
STATE-OWNED ENTERPRISE REFORM SUPPORT PROGRAM
(EC-L1251)

<table>
<tr><th colspan="5">Financial Terms and Conditions</th></tr>
<tr><td colspan="3" rowspan="2">Borrower: Republic of Ecuador</td><th colspan="2">Flexible Financing Facility[a]</th></tr>
<tr><td>Amortization period:</td><td>25 years</td></tr>
<tr><td colspan="3" rowspan="2">Executing agency: Ministry of Economy and Finance
Subexecuting agencies: State-owned Enterprise Holding Company (EMCO) (or the entity that replaces it), Ministry of Energy and Nonrenewable Natural Resources (MERNNR), Ministry of Transportation and Public Works (MTOP), Petroecuador, Petroamazonas, Corporación Eléctrica del Ecuador (CELEC), Corporación Nacional de Electricidad (CNEL), and the Ecuadorian National Airline (TAME)</td><td>Disbursement period:</td><td>4 years</td></tr>
<tr><td>Grace period:</td><td>5.5 years [b]</td></tr>
<tr><th rowspan="2">Source</th><th rowspan="2">Amount (US$)</th><th rowspan="2">%</th><td>Interest rate:</td><td>LIBOR-based</td></tr>
<tr><td>Credit fee:</td><td>[c]</td></tr>
<tr><td>IDB (Ordinary Capital):</td><td>75,000,000</td><td>95.13</td><td>Inspection and supervision fee:</td><td>[c]</td></tr>
<tr><td>Local:</td><td>3,840,000</td><td>4.87</td><td>Weighted average life:</td><td>15.08 years</td></tr>
<tr><td>Total</td><td>78,840,000</td><td>100.0</td><td>Approval currency:</td><td>United States dollar</td></tr>
</table>

<table>
<tr><th colspan="6">Project at a Glance</th></tr>
<tr><td colspan="6">Project objective/description: The general objective is to reduce the tax burden on the State arising from its ownership of State-owned enterprises (SOEs). The specific objectives are to: (i) increase the number of SOEs that adhere to the corporate governance principles of the Organisation for Economic Co-operation and Development (OECD), including fiscal governance comparable to that of the private sector; and (ii) increase the efficiency of SOEs in the oil and gas, electricity, and aviation sectors.</td></tr>
<tr><td colspan="6">Special contractual conditions precedent to the first disbursement of the loan: The special contractual conditions precedent to the first disbursement will be as follows: (i) the borrower, through the executing agency, has presented evidence that resources have been allocated and the core staff needed to set up the management team are in place; and (ii) the borrower, through the executing agency, has presented evidence that the corresponding Program Operating Regulations have been approved by the executing agency and the subexecuting agencies and have entered into force under the terms previously agreed upon with the Bank (paragraph 3.7).
Special contractual conditions for execution: (i) prior to execution of the activities that are the responsibility of the subexecuting agencies, evidence will have been received that the respective subsidiary agreements have been signed with those subexecuting agencies on execution responsibilities and the transfer of resources; and (ii) prior to the execution of activities to finance severances under the SOEs' responsibility in Component 2, evidence will have been received that performance agreements have been signed with those SOEs (with or without restitution of funds), and that financial audits have been performed to determine the amounts to be executed (paragraph 3.8).</td></tr>
<tr><td colspan="6">Exceptions to Bank policies: None.</td></tr>
<tr><th colspan="6">Strategic Alignment</th></tr>
<tr><td>Challenges:[d]</td><td>SI ☐</td><td></td><td>PI ☑</td><td></td><td>EI ☐</td></tr>
<tr><td>Crosscutting themes:[e]</td><td>GD ☑</td><td></td><td>CC ☐</td><td></td><td>IC ☑</td></tr>
</table>

[a] Under the terms of the Flexible Financing Facility (document FN-655-1), the borrower has the option of requesting changes to the amortization schedule as well as currency, interest rate, and commodity conversions. The Bank will take operational and risk management considerations into account when reviewing such requests.

[b] Under the flexible repayment options of the Flexible Financing Facility, changes to the grace period are permitted provided that they do not entail any extension of the original weighted average life of the loan or the last payment date as documented in the loan contract.

[c] The credit fee and the inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with the applicable policies.

[d] SI (Social Inclusion and Equality); PI (Productivity and Innovation); and EI (Economic Integration).

[e] GD (Gender Equality and Diversity); CC (Climate Change and Environmental Sustainability); and IC (Institutional Capacity and Rule of Law).

I. DESCRIPTION AND RESULTS MONITORING

A. Background, problem addressed, and rationale

1.1 The macroeconomic imbalances that were triggered by the collapse of oil prices in 2014 continue to constrain Ecuador's economic performance. The price of Ecuadorian blend crude oil dropped from an average of US$97.5 per barrel in 2011-2013 to US$40.8 per barrel in 2015-2017.[1] Oil previously accounted for 50% of Ecuador's exports and almost a third of the income of its nonfinancial public sector (NFPS).[2] In response to the steep price fall, the government cut public investment by three percentage points of GDP in 2015. The oil price shock found Ecuador with very limited fiscal headroom, since large overall deficits had been recorded in 2013 and 2014 (4.6% and 5.2% of GDP respectively).[3] Despite the spending cuts, the revenue reduction resulting from the lower price of crude oil caused the overall deficit to widen to 8.2% of GDP in 2016.[4] In the following year, the authorities implemented new austerity measures which, assisted by a partial recovery of the price of crude (which averaged US$60 per barrel in 2018 and the first quarter of 2019),[5] reduced the NFPS deficit to 4.5% of GDP in 2017 and then to 0.9% in 2018. The consolidated public debt represented 46.5% of GDP in July 2018, compared to 38.6% in 2016.[6] If other liabilities[7] are included in the calculation, the debt amounted to 56% of GDP in July 2018. The fiscal tightening is starting to show through in the social indicators, with the poverty rate up from 22.5% in 2015 to 23.2% in 2018 and extreme poverty increasing from 7.7% to 8.4% in the same period.[8]

1.2 With the aim of restoring fiscal stability on a sustained basis, in 2019 the government has embarked on a fiscal adjustment program to improve the NFPS's nonoil primary balance, including fuel subsidies, from -5.3% of GDP in 2018 to -0.3% in 2021. This move aims to reduce the NFPS public debt from 46.1% of GDP in 2018 to 40% in 2022.[9] On the expenditure side, the adjustment includes structural reforms to reduce the cost of fuel subsidies and pare back the NFPS wage bill; the prioritization of current expenditure on goods and services and investment; and a reduction of the State's fiscal burden arising from its ownership of SOEs. On the income side, the adjustment involves tax reform. These measures will be complemented by reforms to restore the independence of the Central Bank of Ecuador (BCE) and strengthen the financial sector and the labor market, while maintaining and improving social assistance services for the poor and vulnerable. Overall, the government's reform program aims to recalibrate the country's growth drivers, acting as a catalyst for the private sector, and making the economy more

---

[1] Central Bank of Ecuador (BCE), 2019.

[2] Idem.

[3] BCE.

[4] Idem.

[5] Idem.

[6] Idem.

[7] Liabilities that have only recently been included in public debt statistics (Treasury Certificates (Cetes), floating debt, and other obligations related to the oil sector).

[8] National Institute of Statistics, 2019.

[9] International Monetary Fund (IMF), 2019. *Staff Report. Extended Fund Facility for Ecuador.*

competitive. The program has been supported by the International Monetary Fund (IMF), the Bank, and other multilateral agencies.

1.3 **The fiscal importance of the SOEs.** The fiscal consolidation underscores the need, expressed in the 2018-2021 Prosperity Plan, to evaluate and address the risks associated with the management of SOEs. There are 22 SOEs within the executive branch structure,[10] 256 that are attached to decentralized autonomous governments, and 18 associated with public universities.[11] The State-owned Enterprises Act (LOEP) authorized the creation of a State-owned Enterprise Holding Company (EMCO), as the owner of the SOEs and with responsibility for their strategic planning. The Ministry of Economy and Finance (MEF) is in charge of public finance as it pertains to the SOEs, which it coordinates through the National State-owned Enterprise Directorate (DNEP).

1.4 In 2018, SOEs within the executive branch structure had a permanent workforce of around 39,000 (about 8% of all NFPS public employees), assets of US$47.602 billion (45.3% of GDP), and a combined net worth of US$36.089 billion (34.4% of GDP).[12] These 22 State-owned enterprises paid wages totaling US$964 million in 2018, which amounted to 9% of the total NFPS payroll and about 0.9% of GDP.[13] They generated roughly 32% of the NFPS's total income in 2000-2018, of which 28 percentage points was obtained from oil (Figure 1).[14] The budgetary appropriations needed to run these SOEs amounted to approximately 4.2% of GDP in 2018; and their combined operating earnings, generated mainly by the oil companies, averaged 1.4% of GDP between 2000 and 2018 (Figure 2). The nonoil SOEs posted deficits averaging 1% of GDP during this period.

[10] The 22 are: Ferrocarriles del Ecuador, Flota Petrolera Ecuatoriana (FLOPEC), Correos del Ecuador, TAME, Corporación Nacional de Telecomunicaciones (CNT), Empresa Nacional de Minería, Medios Públicos, Empresa Pública del Agua, Unidad Nacional de Almacenamiento, Santa Barbara, Centros de Alto Rendimiento, Astinave, Corporación Nacional de Electricidad (CNEL), Corporación Eléctrica del Ecuador (CELEC), Fabricamos Ecuador (FABREC), Empresa Pública Cementera, Yachay, Enfarma, Ecuador Estratégico, Casa para Todos, Petroecuador, and Petroamazonas.

[11] MEF, 2019.

[12] EMCO, 2019.

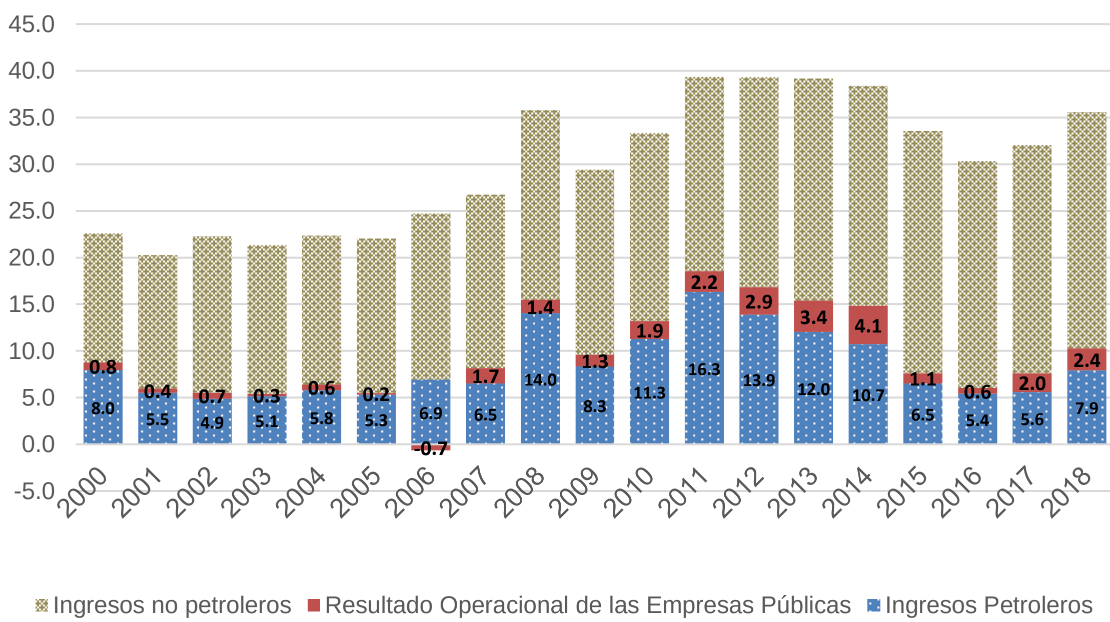
[13] MEF, 2019.

[14] BCE, 2019.

Figure 1. Share of SOEs in NFPS income

Source: BCE.

Figure 2. NFPS income (% of GDP)



Source: BCE.

1.5 Ecuadorian SOEs post weak results in terms of financial performance. Roughly half of them reported losses on average during 2010-2016;[15] and, apart from the oil companies, they are a drain on NFPS cash flows. The SOEs within the

[15] Musacchio A. and Pineda E., 2019. *Fixing State-Owned Enterprises: New Policy Solutions to Old problems.* IDB.

executive branch structure have the third most negative cash flow in the region (-0.61% of GDP), after Jamaica (-0.99%) and Honduras (-1.02%). If the oil companies are included, however, Ecuador's SOEs as a whole generate a positive cash flow equivalent to 3.29% of GDP, the highest in the region ahead of Panama (3.02%).

1.6 The State covers SOE losses by making transfers from the General State Budget (PGE). This relieves the enterprises of the need to be financially self-sustainable and removes hard budgetary constraints. Ecuador has transferred more funding to its SOEs than any other country in the region (2.17% of GDP on average from 2010 to 2016) and far more than the regional average. A large proportion of these transfers is used to support the SOEs' high wage structure, which is above that of the rest of the NFPS. Public sector wages have grown by 78% since 2007 and, on average, are double those of their private-sector peers.[16]

1.7 **The technical framework of the reform.** The government's SOE reform strategy cites the Organisation for Economic Co-operation and Development (OECD) guidelines on SOE ownership and corporate governance as its technical framework.[17] These guidelines are developed in detail around seven principles: (i) rationales for state ownership; (ii) the state's role as an owner; (iii) SOEs in the marketplace; (iv) equitable treatment of shareholders and other investors; (v) stakeholder relations and responsible business; (vi) disclosure and transparency; and (vii) the responsibilities of the boards of SOEs. Under the evaluative framework of the OECD principles of ownership and corporate governance, the government has identified a number of structural reforms to its SOE management regime that will be addressed through this operation and the policy-based loan Program to Support the Improvement of Fiscal Management and Economic Development (paragraph 1.13).

1.8 The key problem identified is the fiscal burden imposed on the State by its ownership of SOEs. In 2018, the budgetary appropriations needed to run the SOEs within the executive branch structure was estimated at roughly 4.2% of GDP, and the SOE wage bill amounted to 0.9% of GDP.[18] The NFPS posted a surplus from the SOEs of around 1.4% of GDP in the period 2000-2018, thanks to the earnings of the oil companies and the national telecom operator, Corporación Nacional de Telecomunicaciones (CNT). In contrast, the rest of the group generated an average deficit of 1% of GDP during that period.[19] The specific problems and their drivers are described below:

1.9 **Weak corporate and fiscal governance.** The regulatory and institutional frameworks are inadequate for managing SOEs:

a. **Inadequate regulatory framework:** (i) the regulatory framework is not aligned with the best international standards of corporate governance (LOEP),[20] because it does not separate the functions of public policy, ownership, and

[16] MEF, 2018.

[17] OECD, 2016. *OECD Guidelines on Corporate Governance of State-Owned Enterprises*, Éditions OECD.

[18] MEF, 2019.

[19] DNEP, 2018.

[20] OECD, 2016.

administrative management[21] (the firms do not have professional boards of directors, and sector ministers chair the boards, which diminishes the separation of functions and results in less frequent meetings). The framework also allows for detrimental discretion in creating and changing the SOEs' line of business.[22] The LOEP does not have enabling regulations; (ii) women are virtually absent in top management bodies. Of the 66 SOE board positions, only two are occupied by women, and only because of their appointment as ministers beforehand; (iii) the SOE tax regime is not comparable to that of private companies,[23] thereby establishing an environment of unequal competition, since SOEs are exempt from corporate income tax on their net earnings; and the tax regime does not provide incentives to partially reinvest dividends in the growth of the enterprise, but allows any surplus produced to be absorbed into the public coffers;[24] and (iv) SOE transparency standards are also not aligned with best practices in several fundamental respects: (a) as SOEs are exempt from paying income or similar taxes, they are not required to file income tax returns that are audited by the Internal Revenue Service (SRI); and the SRI has not developed specific capacity to facilitate the taxation of SOEs under this instrument; and (b) as they are not legally required to do so, most SOEs do not publish up to date financial statements[25] that have been produced and audited according to international accounting standards, which makes it difficult to estimate their definite and contingent liabilities.

b. **Institutional and governance weakness:** (i) EMCO, which is a public company with no commercial aims, assumes SOE management functions that should not fall under its mandate per international best practices. It is overstaffed,[26] and its competencies overlap with those of the MEF and SOE boards of directors.[27] Furthermore, there is a lack of efficient SOE performance evaluation mechanisms that enable rigorous monitoring of the fulfillment of their objectives while guaranteeing sufficient board autonomy; (ii) the DNEP has insufficient resources and management tools to regulate budgetary

[21] All told, 21% of all meetings were ordinary meetings (2017), while 72% were special or urgent meetings. Escobar, B. *Optimización del Rendimiento de Empresas Públicas de Ecuador*, IDB 2018.

[22] Several SOEs made investments outside of their line of business that had an impact on their balance sheets. Examples include the construction of the Monteverde Terminal or the Esmeraldas Pier by Flota Petrolera Ecuatoriana (FLOPEC). Fabricamos Ecuador (FABREC) also has highly varied lines of business, including the textile industry and vehicle importation, and it was authorized to alter the items autonomously. Escobar, B., 2018.

[23] IDB, 2007. *Identifying and Mitigating Fiscal Risks from State Owned Enterprises* (SOEs). *Discussion Paper* IDB-DP-546; and Wagner R.A., M. Jara-Bertin, and A. Musacchio (2015). *Implicit Bailouts and the Debt of Wholly State-Owned Enterprises. Discussion Paper.*

[24] SOE surpluses are transferred to the MEF under a discretionary system that generates transaction costs. International experience shows that the absence of a rules-based tax regime is associated with a soft budget constraint that encourages inefficiency in SOEs. Ter-Minassian, 2017; Musacchio, Pineda and Garcia, 2015.

[25] The Office of the Comptroller General (CGE) hires external auditors to audit the SOEs' financial statements. The service is not provided in a timely manner: it is not tendered on time and often the auditors do not issue an opinion on the financial statements.

[26] It has a staff of 71 to manage 22 SOEs. In contrast, the Chilean system, which is an example of good management practices for SOEs in the region, manages 20 SOEs with 23 employees.

[27] Escobar, B. (2018).

processes between the MEF and the SOEs:[28] (a) the DNEP does not have payment capacity certification systems; (b) it does not have timely and adequately structured information on the SOEs' financial statements and production statistics; (c) it lacks analytical tools to estimate production costs in strategic sectors, such as electricity or oil and gas; and (d) it does not have sector specialists in areas that are strategic for the State; and (iii) the decentralized autonomous governments have insufficient resources and tools to manage their SOEs and prepare financial information to report to the MEF. The register of SOEs attached to decentralized autonomous governments and universities is not updated regularly and does not include information other than the SOE's official and business names.[29]

1.10 **Deficient management of the SOEs.** An analysis of the portfolio of the 22 SOEs within the executive branch structure reveals poor financial performance resulting from multiple causes:[30]

a. The SOEs of greatest fiscal importance, namely the oil companies Petroamazonas (PAM) and Petroecuador (PEC), employ about 30% of the staff of all SOEs within the executive branch structure; and they account for 40% of their capital value. Technical efficiency indicators are inferior to those of their international peers. The ratio of income to number of employees places the two Ecuadorian companies (combined) below the levels of the most efficient oil companies. This is explained by: (i) misalignment between the sector's strategy and the country's energy matrix; (ii) the distinction that is drawn between upstream processes (exploration and extraction), midstream processes (transportation), and downstream processes (marketing and refining), dividing them among several companies (with Petroamazonas responsible for upstream processes and Petroecuador for downstream processes), which is unusual among modern oil companies and can generate inefficiencies;[31] and (iii) weaknesses in corporate management, fiscal regime, and transparency that are common to the sector.

b. Weak coordination of electricity generation, transmission, and distribution activities (between CELEC, CNEL, and other power distribution companies) generates technical inefficiencies, and these companies face the same corporate governance and tax challenges as all SOEs.

c. Management of Ecuador's national airline, TAME, poses major challenges. Unlike similar airlines elsewhere,[32] it does not have automated management systems; it internalizes processes that are generally outsourced (such as baggage handling, ground handling, or security services); and it has posted losses averaging US$73 million (2013-2018), which are covered by State

[28] Budget negotiations are not based on adjusted estimates of production costs or reliable revenues. The processes are defined by Ministerial Agreement 100.

[29] DNEP, 2019.

[30] Idem.

[31] Based on similar processes in the industry, the Ministry of Energy and Non-Renewable Natural Resources (MERNNR) estimates that the merger could increase the profit margin by around US$300 million annually.

[32] U.S. regional carriers with single-aisle aircraft operating domestic routes (Southwest, JetBlue, and Spirit).

transfers.[33] In operational terms, the airline has 127 employees per aircraft, compared to an average of 85 in similar companies.[34]

d. In terms of human talent, the 22 SOEs employ 39,000 civil servants, who receive an average wage that is 40% higher than that of private-sector firms, amounting to close to 1% of national GDP (MEF, 2018). Compared to leading industries, SOEs in strategic sectors are overstaffed. The income-to-staff ratio in oil companies (1.0 for Petroecuador and Petroamazonas combined) is below that of the sector leaders (Ecopetrol reports a ratio of 2.49, and global leaders such as Royal Dutch Shell or BP plc have ratios above 4.0).[35] Initial government estimates show that a merger of these two companies could produce resource savings of 4%-6% of their total costs.[36] SOEs also face resource constraints for financing severance pay; and the absence of budgetary mechanisms hinders provisioning for such payments in the future. Layoff processes do not adhere to systematic planning that would help define the required human talent flows (quantity and profiles) based on the SOEs' strategic planning.

e. Possible resistance to implementation of the reform both from staff affected by the changes and from the public at large, owing to a lack of knowledge of the objectives of the SOE reform and its benefits for the companies, the State, and the public at large.

1.11 **International evidence and lessons learned.** SOEs play a major role in developing countries, where, in many cases, they provide basic services such as electricity, water, and transportation. In Latin America and the Caribbean, the value of SOE assets is estimated at 12% of regional GDP.[37] Despite their economic importance, SOEs can pose a number of problems, particularly overstaffing and the generation of fiscal costs and risks, given their public-ownership status.[38] For example, Bova et al (2016) found that SOE contingent liabilities represented 14% of the total contingent liabilities of the 80 countries in the sample analyzed, while the fiscal costs of SOE bailouts averaged 3% of GDP. For Latin America and the Caribbean, Musacchio and Pineda (2019) estimate the value of these liabilities at 9.14% of GDP. International experience shows that centralized SOE oversight mechanisms, in conjunction with a rules-based fiscal relationship, are associated with better performance and lower fiscal risks.[39]

1.12 **The Bank's experience.** The Bank has supported various initiatives to strengthen SOE governance in Latin America and the Caribbean, through the following operations: (i) ATN/KR-14970-RG for a diagnostic assessment of the fiscal impact and transparency of SOEs; (ii) ATN/KR-14602-RG for the reform of the Latin American Network on Corporate Governance of State-owned Enterprises; and (iii) ATN/KR-16851-RG to strengthen the institutional capacity of SOEs by

---

[33] MEF, 2019.

[34] Massachusetts Institute of Technology, 2019. *Airline Data Project.*

[35] *Offshore Technology*, 2019. Corporate websites.

[36] Ministry of Energy and Nonrenewable Resources, 2019.

[37] Moreno de Azevedo Sánchez, 2016.

[38] For a comprehensive discussion of the topic, see Ter-Minassian (2017).

[39] Musachio A. and E Pineda. *Fixing State Owned Enterprises: New Policy Solutions to Old Problems*, IDB, forthcoming.

improving their fiscal discipline. In Argentina, the Bank has supported reforms implementation (operation ATN/OC-16115-AR), and optimization of the efficiency of public investment by SOEs (loan 4569/OC-AR). In Colombia, it has supported SOE management strengthening through an asset management strategy and performance appraisal mechanisms (loan 4552/OC-CO and technical cooperation operation ATN/OC-17173-CO). The design of this program incorporates the following lessons learned from these operations: (i) the need to align the fiscal framework of SOEs with that of their private-sector counterparts, in order to create a level playing field; (ii) the need for professionally qualified boards of directors with execution capacity that are free from political interference; and (iii) the need to make SOEs subject to transparent and public management performance indicators, within an adequate degree of financial and operational autonomy.[40] In Ecuador, the Bank has contributed to programs aimed at optimizing human talent in the public sector, such as the recent loan 4364/OC-EC. The lessons learned from implementation of that operation that have informed the design of this one include: (i) linking the financing of severance pay to the beneficiary entities' optimization plans; (ii) financing legally required severance payments as benefits, but not overdue wage payments; (iii) prioritization of voluntary and *force majeure* layoffs over job elimination; (iv) conducting of independent financial audits prior to disbursements of the loan proceeds; and (v) verification of the objectives of SOE human talent profiling through layoffs and by hiring the necessary staff.

1.13 **Complementarity with other Bank operations.** In 2019, the Bank has approved a special development loan (SDL) for US$500 million (Emergency Program for Macroeconomic Sustainability and Prosperity, loan 4771/OC-EC) and a policy-based loan (Program to Support Improved Fiscal Management and Productive Development, loan 4825/OC-EC) in the area of fiscal policy. The Bank is also processing an investment loan to support improved efficiency in tax management in addition to this operation.[41] This investment loan supports the implementation of SOE institutional policy reforms, one of the PBL policy measures,[42] thus affording medium-term sustainability to the structural reforms defined by the government. The Bank is the leading multilateral organization supporting reform of the SOE system.

1.14 **Strategic alignment.** The program is aligned with the Update to the Institutional Strategy 2010-2020 (document AB-3008), and with the challenge of productivity and innovation, as it provides a level playing field to facilitate the efficient operation of SOEs. It is also aligned with the cross-cutting themes of: (i) gender equality and diversity, by increasing women's participation in leadership positions in the public sector; and (ii) institutional capacity and the rule of law, by strengthening

[40] With operation 1925/OC-EC, the Bank facilitated integration and connectivity in Ecuador, among the country's most isolated and disadvantaged areas, through improvements in commercial air transportation services and operations by renewing TAME's fleet of aircraft and strengthening its business capacity.

[41] The government's structural reform program has been supported by an IMF Extended Fund Facility (EFF) arrangement for 2019-2021. The IMF will disburse approximately US$4.2 billion over three years, and international agencies will provide supplementary financing of up to US$6 billion, of which the Bank would provide roughly US$1.68 billion in new approvals between 2019-2021.

[42] The policy matrix includes measures financed by this operation: (i) reform of the LOEP; (ii) implementation of reforms to the SOE fiscal regime; (iii) a new institutional framework that ensures good corporate governance practices; and (iv) government approval of the oil companies merger strategy.

institutional, technical and, financial capacities for the management of SOEs. The program will also contribute to the 2016-2019 Corporate Results Framework (document GN-2727-6) through the output indicator of government agencies benefited by projects that strengthen technological and managerial tools to improve public service delivery. It is aligned with the Sector Strategy on Institutions for Growth and Social Welfare (document GN-2587-2) through its support for the improvement of public expenditure quality. It is also consistent with the Fiscal Policy and Management Sector Framework Document (document GN-2831-8), which stresses the importance of institutional strengthening to improve public spending quality; and also with the Gender and Diversity Sector Framework Document (document GN-2800-8) as it will strengthen women's voice and agency by promoting their leadership in the public sector. The program is aligned with the IDB Group's Country Strategy with Ecuador 2018-2021 (document GN-2924), through the strategic objectives of generating efficiencies and increasing the quality of public expenditure, and boosting the contribution of private investment and productivity to economic growth. The operation is included in the 2019 Operational Program Report (document GN-2948); and it is aligned with the government's 2018-2021 Prosperity Plan and 2017-2021 Development Plan as it contributes to the optimization of public spending.

B. Objectives, components, and cost

1.15 The general objective is to reduce the tax burden on the State arising from its ownership of State-owned enterprises (SOEs). The specific objectives are to: (i) increase the number of SOEs that adhere to OECD corporate governance principles, including fiscal governance comparable to that of the private sector; and (ii) increase the efficiency of SOEs in the oil and gas, electricity, and aviation sectors. These objectives will be achieved through the following components and activities:

1.16 **Component 1. Strengthening of the SOE corporate governance and fiscal framework (US$4.6 million)**.

a. **Subcomponent 1.1. Improvement and implementation of the regulatory framework.** (i) Regulatory framework. The following activities will be financed: (a) actions to raise public awareness about the new LOEP,[43] [44] [45] including targets for women's participation on SOE boards of directors; (b) preparation of regulations for the LOEP; (c) verification of LOEP implementation and preparation of the associated technical standards; and (d) training for public officials and employees on the LOEP reforms; (ii) Fiscal governance regime.[46] The following activities will be financed: (a) design of the SOE revenue collection function in the Internal Revenue Service (SRI) and training for SRI staff; (b) design of the SOE tax function and training for SOE employees to assume tax responsibilities; and (c) design of the tax regime for companies in

[43] The proposed LOEP reform is being supported by technical cooperation operation ATN/OC-17299-EC.

[44] According to the 2016 OECD Guidelines on Corporate Governance of State-Owned Enterprises.

[45] Measures include: (a) improved corporate governance; (b) a tax regime consistent with that of the private sector; and (c) transparency and accountability requirements.

[46] The design of the fiscal governance regime and the tax regime specific to the oil companies is being supported by technical cooperation operation ATN/OC-17299-EC.

the oil and gas sector; and (iii) Transparency and accountability. The following activities will be financed: (a) training for SOE employees on International Financial Reporting Standards (IFRS) and financial statement reporting; (b) preparation of a report on the criteria for external auditor prequalification; and (c) technical support for SOE ISO-7001 certification.

b. **Subcomponent 1.2. Redesign of the ownership and management functions.** (i) Support for implementation of the SOE holding company to replace EMCO.[47] The following activities will be financed: (a) supervision of measures to implement the new SOE holding company and preparation of its charter; (b) training for the employees of the new entity, including the design of a change management strategy; (c) awareness-raising actions; and (d) design of a performance management contract between the holding company and the SOEs; (ii) strengthening of the DNEP. The following activities will be financed: (a) development of production costing studies and systems to assist budgeting; (b) development of payment capacity certification systems; (c) development of software to generate financial statistics through specialized reporting systems; and (d) training for staff in strategic sectors;[48] and (iii) Support for decentralized autonomous governments. The following activities will be financed: (a) technical assistance to adopt the LOEP reforms in their respective SOEs;[49] and (b) development of a financial sustainability analysis for SOEs that are attached to decentralized autonomous governments.

1.17 **Component 2. SOE portfolio optimization (US$70.8 million).**

a. **Subcomponent 2.1. SOE redesign.** (i) Support for the Petroamazonas-Petroecuador merger. This subcomponent will finance the following activities: (a) preparation of the merger strategy; (b) implementation of the merger (including design and implementation of a change management strategy);[50] (c) technical assistance on the value chain (oil exploration and production) to make the merger more efficient; (d) implementation of the management information system; and (e) legal advice on the merger; (ii) optimization of CELEC and CNEL operations. Funding will be provided for consulting services to include: (a) an institutional diagnostic assessment and a coordinated proposal for management of the electricity sector, including the design of a change management strategy; (b) implementation of the LOEP reforms; and (c) production costing studies, including estimation of asset values; and (iii) Appraisal of TAME assets. The following activities will be financed: (a) an assessment as to whether State ownership is appropriate, market analysis, and commercial exploitation strategy;[51] and (b) preparation of financial statements in accordance with the 2017-2018 IFRS.

---

[47] The design of the new SOE holding company will be supported by technical cooperation operation ATN/OC-17299-EC.

[48] DNEP and MEF technical staff, in the oil and gas, electricity, and telecommunications sectors.

[49] Public awareness-raising and training actions.

[50] The merger will require legal support to adapt the strategy proposed by the company to national regulations.

[51] The consulting services started in February 2019.

b. **Subcomponent 2.2. Improved management and optimization of human talent.** This subcomponent will finance the following: (i) severances for staff laid off as a result of the optimization consultancies financed by the program, at EMCO, Petroecuador, Petroamazonas, CELEC, CNEL, and TAME.[52] To this end, support will be provided to fund the following priority severance types:[53] (a) mandatory retirement due to age (over 70);[54] (b) voluntary resignation due to catastrophic illness or disability;[55] (c) voluntary resignation;[56] and (d) layoffs due to elimination of positions,[57] [58] which must comply with the eligibility and other requirements established for this purpose in the program Operating Regulations. These severance types are guaranteed under current law (the Public Service Act (LOSEP) and the LOEP).[59] These severance arrangements will benefit approximately 3,350 employees of the SOEs in question; and (ii) implementation of the public and internal communication strategy to facilitate understanding of the reform and its benefits for citizens.[60]

1.18 **Program administration and contingencies (US$3.4 million).** Financing will be provided to cover administrative expenses incurred by the executing agency, program evaluations, and audits. An amount is included for contingencies.

1.19 **Beneficiaries.** The program will benefit: (i) the central government and decentralized autonomous governments, directly, through better management of public resources; and (ii) the population at large, indirectly, by contributing to greater efficiency in the delivery of goods and services; and the private sector, which will indirectly benefit from structural reforms in the SOE areas by facilitating a level playing field that enables the SOEs to operate efficiently and is conducive to business development. In addition, MEF staff will benefit directly as users, through the development of management instruments and training in strategic sectors; as will SRI staff who will receive training for their role of collecting taxes from SOEs; and also the SOE staff themselves, who will receive training to fulfill their tax responsibilities and implement IFRS and SOE financial statement reporting.

---

52 The layoffs are expected to improve the SOEs' performance, since the consulting services for this activity will help upgrade the SOEs' human talent profile, particularly in terms of the posts needed to optimize their management and operations.

53 This expenditure is consistent with the Modernization of Policies and Practices that Restrict the Use of Resources in Investment Loans (document GN-2331-5), and with the country finance parameters agreed upon with Ecuador (document CP-28273 and Annex IX of document GN-2495).

54 Article 81 of the LOSEP, Article 289 of the LOSEP Regulations, and Article 188 of the Social Security Act (LSS) – Old-age retirement.

55 Article 186 of the LSS – Disability Retirement.

56 Article 288 of the LOSEP Regulations.

57 Articles 23 and 60 of the LOSEP and Article 30 of the LOEP.

58 Support for other types of severances prescribed for by national legislation will be contingent on their consistency with the country's laws and constitution and will conform to the criteria and objectives set forth in the program analysis, subject to the Bank's prior no objection. The program Operating Regulations will contain a detailed description of each severance type to be financed. Priority will be given to those that contribute to generational change in education and to a change in the SOE human talent profile.

59 The LOEP refers to the Labor Code.

60 The design will be supported by technical cooperation operation ATN/OC-17299-EC.

C. Key results indicators

1.20 **Expected results.** The program's expected impact is a reduction of the State's fiscal burden from SOE ownership, measured as the total amount of budgetary appropriations-transfers from the PGE to the SOEs (relative to GDP), from 4.2% in 2018 to 3.2% in 2022. The main outcomes will be: (i) an increase in the percentage of the total number of SOE board meetings that are regular meetings, from 21% in 2017 to 70% in 2022; (ii) an increase in the percentage of SOEs with up-to-date audited financial statements, from 13.6% in 2018 to 100% in 2022; (iii) an increase in women's participation on SOE boards of directors from 3% in 2018 to 40% in 2022; and (iv) an increase in productive efficiency as measured by reductions in the following ratios: (a) payroll expenses per barrel of oil equivalent, from 1.20 in 2018 to 1 in 2022 (Petroamazonas); (b) payroll expenses relative to oil derivatives or refined products produced, from 1.85 in 2018 to 1.77 in 2022 (Petroecuador); (c) the number of employees relative to output (GWh), from 0.22 in 2018 to 0.15 in 2022 (CELEC); (d) the number of employees per thousand customers, from three in 2018 to two in 2022 (CNEL); and (e) the number employees per aircraft from 128 in 2018 to 85 in 2022 (TAME).

1.21 **Economic rationale.** An economic analysis was made of the program's economic/financial costs and benefits. By the end of 2028 (10 years from the start of program execution) the investments will have generated an estimated net present value (NPV) of US$60.04 million, with an internal rate of return (IRR) of 33%. These results are robust to the sensitivity analysis performed. The economic benefits generated by the program materialize in the form of savings (costs avoided) due to increased efficiency in the merger of the oil companies, greater transparency in the SOEs due to their alignment with OECD principles; and savings obtained from staff layoffs resulting from optimization processes in EMCO, Petroecuador, Petroamazonas, CELEC, CNEL and TAME. The economic costs take the form of the program's capital expenditures and operating expenses, which include the amounts assigned to the merger of the oil companies, the consulting services to optimize CELEC and CNEL, the appraisal of and commercial exploitation strategy for TAME, staff severance payments, and operating expenses, measured in terms of efficiency prices.

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instruments

2.1 This program will consist specific investment loan for a total amount of US$78.84 million, financed with US$75 million from the Bank's Ordinary Capital and a local counterpart contribution of US$3.84 million from the Republic of Ecuador. The local counterpart will be obtained by levying a value added tax (VAT) on the activities financed (see table 1 and the itemized budget).

Table 1. Total budget (US$)

Categories	IDB	Local	Total	%
1. Direct costs	71,926,346	3,471,161	75,397,507	95.63
Component 1. Strengthening of the SOE corporate governance and fiscal framework	4,109,946	493,193	4,603,139	5.84
Subcomponent 1.1. Improvement and implementation of the regulatory framework	2,922,426	350,691	3,273,117	4.15
Subcomponent 1.2. Redesign of the ownership and management functions	1,187,520	142,502	1,330,022	1.69
Component 2. SOE portfolio optimization	67,816,400	2,977,968	70,794,368	89.79
Subcomponent 2.1. SOE redesign	24,262,000	2,911,440	27,173,440	34.47
Subcomponent 2.2. Improved management and optimization of human talent	43,554,400	66,527	43,620,928	55.33
2. Program administration	1,610,600	193,272	1,803,872	2.63
3. Contingencies	1,463,054	175,567	1,638,621	1.74
Total	**75,000,000**	**3,840,000**	**78,840,000**	**100**

2.2 **Disbursement scheduling.** Disbursements will be spread over a maximum of four years, since high-value activities (the consulting services for the oil companies' merger and the public employee layoff process) are already being implemented and require a large portion of the loan proceeds to be disbursed in 2020:

Table 2. Disbursement schedule (US$)

Source	Year 1	Year 2	Year 3	Year 4	Total
IDB	2,771,074	58,166,749	11,340,479	2,721,699	75,000,000
Local	332,529	1,820,010	1,360,857	326,604	3,840,000
Total	**3,103,603**	**59,986,759**	**12,701,336**	**3,048,303**	**78,840,000**
%	**3.94**	**76.09**	**16.11**	**3.87**	**100**

B. Environmental and social risks

2.3 As no socioenvironmental risks are anticipated because the program will not finance works or infrastructure, the program has been classified as a Category "C" operation, pursuant to Directive B.3 of the Bank's Environment and Safeguards Compliance Policy (document OP-703).

C. Fiduciary risks

2.4 The following medium-high fiduciary risks were identified: (i) delays in program implementation due to insufficient technical staff at the executing agencies, owing to high turnover rates, compounded by a lack of staff with experience in implementing programs with multilateral agencies. As a mitigation measure, the MEF team needs to be reinforced with the following, at least: a program coordinator, a financial specialist, a procurement specialist, and a planning and monitoring specialist, to serve from the start of execution through to loan closure; and (ii) difficulties in monitoring the funds disbursed to the different executing units and delays in program implementation owing to participation by multiple entities, some of which are outside the central government domain. As a mitigation measure, the execution mechanism calls for the MEF to coordinate and centralize all information; contracting and payments pertaining to activities that benefit the

SOEs to be handled by the line ministries, which are part of central government; and SOE staff severance payments to be made through reimbursements rather than advances of funds.

D. Other key issues and risks

2.5 A risk management workshop was held, following the Bank's methodology. Risks classified as medium-high are listed below:

a. **Public management and governance.** The following risks are rated medium-high:

(i) Turnover among the authorities that results in changes to public policy priorities and holds up approval of the LOEP reform and, with it, the goals planned up to 2020. This risk will be mitigated by holding discussions with the new authorities on the importance of the reforms, and by activities to raise public awareness of the expected impacts of the measures among citizens at large. The LOEP reform will be included as a measure in the Policy Matrix of the Program to Support Improved Fiscal Management and Productive Development (paragraph 1.13). Lastly, the Extended Fund Facility includes commitments to reform the SOE management framework to enable monitoring to be shared between the IMF and the Bank.

(ii) There could be delays in program execution owing to problems in coordinating the program's different subexecuting agencies. This risk has been mitigated during the design of the operation by holding meetings between the MEF work teams (Legal, Public Financing, Planning, DNEP), EMCO, and the Bank, to support the successful tendering of the planned activities. Interagency agreements between the executing agency and subexecuting agencies specify governance frameworks for implementing program activities that facilitate participation by all entities. Meetings will also be held between the institutions and the Bank's project team to oversee implementation.

b. **Development.** The following risk is rated medium-high:

(iii) There is a risk of implementation problems with the reform based on the economic policy that it advances, due primarily to potential resistance from personnel at the SOEs affected by layoffs and general public opinion on the future quality and coverage of public services. This will be mitigated by contracting consulting services to manage change in processes aimed at optimizing SOE human talent and to inform the public on the phases and milestones of the reform program, and its benefits.[61]

2.6 **Program sustainability.** Actions to support the sustainability of the program's objectives include: (i) development of a new regulatory framework based on the OECD guidelines that introduces fiscal governance and transparency and accountability mechanisms to provide greater clarity in the management of each

[61] The program provides funding for the implementation of a public information campaign on the reform, which operation ATN/OC-17299-EC will also support.

State-owned enterprise, along with certainty and timeliness in their financial information, thereby reducing transaction costs; and (ii) development of a new institutional framework for SOE management, including a proposal for a new coordinating agency/entity, and the definition of program execution responsibilities among government agencies.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

3.1 The borrower will be the Republic of Ecuador, represented by the Ministry of Economy and Finance (MEF). The executing agency will be the MEF, acting through the DNEP. The subexecuting agencies will be: (i) EMCO, or the new entity that replaces it; (ii) the Ministry of Energy and Nonrenewable Natural Resources (MERNNR); (iii) the Ministry of Transportation and Public Works (MTOP); and (iv) the Petroecuador, Petroamazonas, CELEC, CNEL, and TAME SOEs. The MEF has served as executing agency in the following operations: 3073/OC-EC, 3726/OC-EC, 4614/OC-EC, 4670/OC-EC, and 4364/OC-EC; and it has experience in executing Bank programs. In view of its current workload and the specific nature of the program objectives, the executing agency will be given technical and administrative support to enable it to assume the additional planning, execution, monitoring, and control responsibilities.

3.2 The MEF will be responsible for execution of the entire program and, in particular, together with EMCO (and its eventual successor),[62] for the execution of activities under Component 1. The executing agency will form its management team to ensure the program is implemented as specified in the Program Operating Regulations. The executing agency's core staff will be: (i) a General Coordinator; (ii) a Financial and Management Coordinator; (iii) a Procurement Officer; and (iv) a Planning, Monitoring, and Evaluation Officer.

3.3 The executing agency's main responsibilities will be to: (i) plan execution of the activities; (ii) prepare, implement, and update the following project management tools: the multiyear execution plan,[63] the procurement plan, the annual work plan, and the progress monitoring report; (iii) supervise execution and submit status reports; (iv) carry out the processes involved in the preparation of terms of reference, goods tendering and procurement, and the selection and contracting of services for the activities under its responsibility; (v) submit supporting documentation and disbursement requests to the Bank; (vi) file audited annual financial statements; (vii) prepare the program evaluation; and (viii) coordinate the government activities needed for program implementation.

3.4 The ministries that will serve as subexecuting agencies (MERNNR and MTOP) will be responsible for the following under Component 2: (i) completing the processes involved in preparing terms of reference, goods tendering and procurement, and the selection and contracting of services for the activities under their responsibility; (ii) providing the MEF with the information necessary for fulfilling the above on a

---

[62] If the new entity does not have contracting authority, the consulting services for SOE output 1.3 would be contracted by the SOE line ministries (MERNNR and MTOP).

[63] The multiyear execution plan and procurement plan were developed in workshops held with the executing units, consolidating procurement processes by product and type.

timely basis; and (iii) planning, monitoring, managing, and reporting to the executing agency on the use made of the financial resources under their responsibility. The SOEs that will serve as subexecuting agencies (EMCO or the entity that replaces it, Petroecuador, Petroamazonas, CELEC, CNEL, and TAME) will be responsible for executing severance-related disbursements financed under the program. The executing agency's management team will support the subexecuting agencies in the operational and fiduciary management of the activities for which they are responsible.

3.5 Program Operating Regulations will also be prepared and will describe the following: (i) the functions, procedures, and rules for implementing the components, specifying the appointment, composition, and functions of the management teams of the executing agency and subexecuting agencies; (ii) the operational and contractual relations between the parties involved in the program; (iii) the mechanism for coordination and transfer of resources between the executing agency and the subexecuting agencies; and (iv) the eligibility criteria for the severance payments.

3.6 **Interagency coordination.** The subexecuting agencies (MERNNR and MTOP) will sign subsidiary financing[64] agreements with the MEF, specifying the activities to be undertaken by the executing agency, as well as the corresponding budgets and the necessary execution, disbursement, monitoring, and evaluation processes. The executing agencies (EMCO, Petroecuador, Petroamazonas, CELEC, CNEL, and TAME) will sign agreements for the fulfillment of objectives[65] (with or without restitution of funds as the case may be), with the MEF specifying the amount of severance-related disbursements to the SOEs,[66] as well as their monitoring and evaluation processes. Strategic coordination will be performed by the owner of the SOEs (EMCO or its successor) and the MEF.

3.7 **Special contractual conditions precedent to the first disbursement of the loan proceeds. The special contractual conditions precedent to the first disbursement will be as follows: (i) the borrower, through the executing agency, has presented evidence that resources have been allocated and the core staff needed to set up the management team are in place (paragraph 3.2)**, this condition being critical to ensure the prompt start of program activities and to avoid delays due to lack of administrative capacity; **(ii) the borrower, through the executing agency, has presented evidence that the corresponding Program Operating Regulations have been approved by the executing agency and the subexecuting agencies and have entered into force under the terms previously agreed upon with the Bank**, this condition being justified insofar as the Operating Regulations will establish guidelines, procedures, and coordination mechanisms for successful program implementation (paragraph 3.5).

3.8 **Special contractual conditions for execution.** (i) prior to execution of the activities that are the responsibility of the subexecuting agencies, evidence will have been received that the respective subsidiary agreements have been signed with those subexecuting agencies on execution responsibilities and the transfer of

64 These will be annexes to the Program Operating Regulations, once signed.

65 Idem.

66 The Bank will reimburse the MEF for payments made (paragraph 3.12).

resources; and (ii) prior to the execution of activities to finance severances under the SOEs' responsibility in Component 2, evidence will have been received that performance agreements have been signed with those SOEs (with or without restitution of funds), and that financial audits have been performed to determine the amounts to be executed.

3.9 **Retroactive financing and recognition of eligible expenditures.** The Bank may provide retroactive financing, as a charge against the loan proceeds, of up to US$15 million (20% of the loan amount) for eligible expenditures incurred by the borrower prior to the loan approval date, in order to engage the consulting services needed to prepare conceptual designs, to establish the execution units, and to cover priority layoffs that are already under way and that being financed with government funds, provided that all such expenditures have met requirements substantially similar to those specified in the loan contract. Expenditures must have been incurred on or after the project profile approval date of 15 February 2019, but under no circumstances may they have been incurred more than 18 months prior to the loan approval date.

3.10 **Procurement.** Procurements financed from the loan proceeds will be made in accordance with Policies for the Procurement of Goods and Works Financed by the Inter-American Development Bank (document GN-2349-9), and the Policies for the Selection and Contracting of Consultants Financed by the Inter-American Development Bank (document GN-2350-9). Procurements in amounts below the international competitive bidding thresholds (US$3 million for works, US$250,000 for goods and nonconsulting services, and US$200,000 in the case of consulting firms) can be processed through Ecuador's National Public Procurement System (SNCP).

3.11 **Financial management and audits.** The provisions of the Financial Management Guidelines for IDB-financed Projects (document OP-273-6) will be applied. Annual program financial statements will be audited by independent auditors acceptable to the Bank and submitted within 120 days following the end of each fiscal year. The last audited financial statement will be submitted no later than 120 days following the date of the final disbursement.

3.12 The Bank will make loan disbursements in the form of advances of funds to meet the project's real liquidity needs according to the financial plan, except for disbursements in respect of staff severance payments. The Bank may also make direct payments to suppliers or reimburse other expenses, at the borrower's request. For disbursements in respect of staff severances, the Bank will reimburse payments made, subject to verification by an independent auditing firm, compliance with legal requirements, and fulfillment of the criteria established in the Program Operating Regulations.

B. Summary of results monitoring arrangements

3.13 **Monitoring** will be based on: (i) the multiyear execution plan and annual work plan; (ii) the procurement plan; (iii) the Results Matrix; (iv) the monitoring and evaluation plan; and (v) the progress monitoring report. Within 30 days following the end of each six-month period, the MEF will send the Bank a semiannual report on progress towards the outcomes, outputs, and financial targets, for approval by the Bank. The Bank will conduct inspection visits and ex post reviews as part of program monitoring.

3.14 **Evaluation.** The program will be evaluated against the annual targets and the outcome and output indicators contained in the program's Results Matrix, through a midterm and a final evaluation using the before-and-after evaluation methodology with attribution of results.[67] An ex post economic evaluation will also be made to ascertain whether the returns envisaged in the ex ante evaluation have materialized. This will be financed from the loan proceeds (monitoring and evaluation plan).[68] The borrower, either alone or through the executing agency, will prepare a midterm evaluation report and submit it to the Bank within 90 days after 60% of the loan funds have been disbursed, or after 30 months of program implementation, whichever occurs first. It will also send the Bank a final evaluation 90 days after the date on which 95% of the loan resources have been disbursed, which will serve as an input for the project completion report.

[67] The result for the treatment group ($Y_{t=1}^{T}\,/T = 1$) is the impact variable measured after the intervention, and the counterfactual ($Y_{t=0}^{C}\,/T = 0$) is defined as the impact variable measured before the intervention.

[68] The MEF will commission these evaluations, and the corresponding terms of reference will be subject to the Bank's approval and no objection.

Development Effectiveness Matrix		
Summary		
I. Corporate and Country Priorities		
1. IDB Development Objectives	**Yes**	
Development Challenges & Cross-cutting Themes	**-Productivity and Innovation -Gender Equality and Diversity -Institutional Capacity and the Rule of Law**	
Country Development Results Indicators	**-Government agencies benefited by projects that strengthen technological and managerial tools to improve public service delivery (#)***	
2. Country Development Objectives	**Yes**	
Country Strategy Results Matrix	**GN-2924**	**Particularly with the objectives of generate efficiences and increase the quality of public expenditure and boost the contribution of private investment and productivity to economic growth.**
Country Program Results Matrix	**GN-2948**	**The intervention is included in the 2019 Operational Program.**
Relevance of this project to country development challenges (If not aligned to country strategy or country program)		
II. Development Outcomes - Evaluability		**Evaluable**
3. Evidence-based Assessment & Solution	**7.7**	
3.1 Program Diagnosis	**3.0**	
3.2 Proposed Interventions or Solutions	**1.7**	
3.3 Results Matrix Quality	**3.0**	
4. Ex ante Economic Analysis	**10.0**	
4.1 Program has an ERR/NPV, or key outcomes identified for CEA	**3.0**	
4.2 Identified and Quantified Benefits and Costs	**3.0**	
4.3 Reasonable Assumptions	**1.0**	
4.4 Sensitivity Analysis	**2.0**	
4.5 Consistency with results matrix	**1.0**	
5. Monitoring and Evaluation	**7.0**	
5.1 Monitoring Mechanisms	**2.5**	
5.2 Evaluation Plan	**4.5**	
III. Risks & Mitigation Monitoring Matrix		
Overall risks rate = magnitude of risks*likelihood	**Medium**	
Identified risks have been rated for magnitude and likelihood	**Yes**	
Mitigation measures have been identified for major risks	**Yes**	
Mitigation measures have indicators for tracking their implementation	**Yes**	
Environmental & social risk classification	**C**	
IV. IDB´s Role - Additionality		
The project relies on the use of country systems		
Fiduciary (VPC/FMP Criteria)	**Yes**	**Financial Management: Budget, Treasury, Accounting and Reporting, External Control, Internal Audit.** **Procurement: Information System, Price Comparison, National Public Bidding.**
Non-Fiduciary		
The IDB's involvement promotes additional improvements of the intended beneficiaries and/or public sector entity in the following dimensions:		
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project	**Yes**	**EC-T1419**

Note: (*) Indicates contribution to the corresponding CRF's Country Development Results Indicator.

Evaluability Assessment Note:

The general objective of the operation is to reduce the fiscal load to the State derived from the proprietorship of Public Enterprises (PPEE). To achieve this goal, the proposal identifies two specific areas to intervene. The first area focuses on increasing the number of PPEE aligned to the corporate governance principles by OCDE. The second area focuses on increasing the efficiency of the PPEE in the energy and aeronautic sectors. The POD includes a description on the amount of transfers from the General State Budget to the PPEE, the gaps in dimensions associated to corporate governance, and the efficiency of the PPEE in the energy and aeronautic sectors.

Regarding the fiscal load, the project proposal quantifies the transfers in 4.2% of GDP (MEF, 2018). Regarding governance, the project identifies only 21% of board sessions are ordinary, 14% of enterprises have updated financial statements (Entidad Propietaria de EEPP, 2018). The diagnostic also identifies a gap in women's participation in boards being 3 women for every 100 men (Entidad Propietaria de EEPP, 2018). Regarding the efficiency of the energy and aeronautic PPEE the diagnostic quantifies expenditures in salaries per unit produced, estimated at values well above those of comparable firms (MERNNR, 2018).

The economic analysis assumes benefits derived from savings induced by improved transparency (via reductions in bribes and inefficient purchases), gains in operating efficiency, and savings associated with the retirement of personnel. The quantified costs include the total amount of the project. The estimated Net Present Value is approximately US $ 60 million and the internal rate of return is estimated at 33 percent. The exercise includes a sensitivity analysis.

Monitoring is based on annual reports from the EEPP, MERNNR, and MTOP. The verification of the delivery of products rests with EMCO, MEF, DNEP, SRI, MERNNR, and MTOP reception certificates. The monitoring plan has a list of annual goals with annual costs. The executing agency is responsible for monitoring. The ex post evaluation to verify the achievement of objectives consists of a reflexive methodology.

Five risks are identified, of which four are classified as medium-high. The medium-high risks identified are changes in authorities, problems of coordination for execution, resistance of the personnel affected, and lack of technical staff given the high turnover of personnel.

RESULTS MATRIX

Project objective:	The general objective is to reduce the tax burden on the State arising from its ownership of State-owned enterprises (SOEs). The specific objectives are to: (i) increase the number of SOEs that adhere to the corporate governance principles of the Organisation for Economic Co-operation and Development (OECD), including fiscal governance comparable to that of the private sector; and (ii) increase the efficiency of SOEs in the oil and gas, electricity, and aviation sectors.

EXPECTED IMPACT

Indicator	Unit of measure	Base-line	Baseline year	2019	2020	2021	2022	Final target	Means of verification	Comments
IMPACT 1: Reduction of the State's fiscal burden from SOE ownership										
Transfers from the General State Budget (PGE) to SOEs / GDP	% US$/US$	4.2	2018	4.2	3.9	3.6	3.2	3.2	Annual Budget Report (MEF)	**Baseline:** 4.2 = Amount of transfers from the PGE to SOEs (US$4.515 billion) relative to GDP (US$107.511 billion)

EXPECTED OUTCOMES[1]

Indicator	Unit of measure	Base-line	Baseline year	2019	2020	2021	2022	Final target	Means of verification	Comments
OBJECTIVE 1: Increase the number of SOEs that adhere to OECD corporate governance principles, including fiscal governance comparable to that of the private sector										
Percentage of total SOE board meetings that are regular meetings	% Number of meetings / Number of meetings	21	2018	21	40	55	70	70	Annual report, SOE holding company	**Baseline**: 21 = Number of ordinary SOE board meetings (11) / Total number of SOE board meetings (53)
SOEs with up-to-date audited financial statements / Total number of SOEs	% Number of financial statements / Number of financial statements	13.6	2018	13.6	20	50	100	100	Annual report, SOE holding company	**Baseline:** 13.6 = Number of SOEs with up-to-date audited financial statements (3) / Total number of SOEs (22)
Number of women on SOE boards of directors / Total SOE board members	% Number of women members / Total number of board members	3	2018	3	15	30	40	40	Annual report, SOE holding company	**Baseline:** 3 = Number of women on SOE boards (2) / Total number of SOE board members (66)

[1] The expected outcomes are cumulative.

EXPECTED OUTCOMES[1]

Indicator	Unit of measure	Base-line	Baseline year	2019	2020	2021	2022	Final target	Means of verification	Comments
OBJECTIVE 2: Increase the efficiency of SOEs in the oil and gas, electricity, and aviation sectors										
Petroamazonas (PAM) payroll expenses / Barrels of oil equivalent produced	Number: US$/ Number of barrels	1.20	2018	1.17	1	1	1	1[2]	Annual report (MERNNR)	PAM labor efficiency. **Baseline:** 1.2 = Payroll expenses (US$178,722,317) / Barrels of oil equivalent (148,461,732)
Petroecuador (PEC) payroll expenses / PEC oil derivatives or refined products produced	Number: US$/ Number of oil derivatives	1.85	2018	1.85	1.82	1.80	1.77	1.77		PEC labor efficiency. **Baseline:** 1.85 = Payroll expenses (US$12,937,748) / Oil derivatives or refined products (6,987,637)
Number of employees of CELEC / CELEC output (GWh)	Number: Number of employees / GWh	0.22	2018	0.22	0.22	0.22	0.15	0.15[3]		CELEC labor efficiency. **Baseline:** 0.22[4] = Number of employees (4,730) / Output (21,370 GWh)
Number of employees of CNEL per thousand CNEL customers	Number: Number of employees / 1,000 customers	3	2018	3	2.5	2.5	2	2[5]		CNEL labor efficiency. **Baseline:** 0.003[6] = Number of employees (6,925) / Thousand customers (2,500)
Number of TAME employees / Number of TAME aircraft	Number: Number of employees / Number of aircraft	128	2018	100	85	85	85	85[7]	Annual Report, MTOP	TAME labor efficiency. **Baseline:** 128[8] = Number of TAME employees (1,150) / Number of aircraft (9)

2 PAM estimates.

3 *Estructura Organizacional y Estatuto Orgánico Funcional por Procesos de CELEC y CNEL* (PricewaterhouseCoopers-PwC, 2014): Average ratio in electric power generation and transmission companies (Interconexión Eléctrica de Colombia, Red Eléctrica Española, and Electronorte de Brasil: 0.056).

4 Accountability report 2018. CELEC website.

5 PwC, 2014: Average ratio in electric power distribution companies (Comisión Federal de Electricidad de México, Empresas Públicas de Medellín, Iberdrola de España: 2).

6 Accountability Report 2018. CNEL website.

7 TAME, 2019: Average of United States regional airlines operating single-aisle aircraft primarily on domestic routes (*Southwest, JetBlue, and Spirit*).

8 TAME, 2019.

OUTPUTS[9]

Indicator	Unit of measure	Base-line	Baseline year	2019	2020	2021	2022	Final target	Means of verification
Component 1: Strengthening of the SOE corporate governance and fiscal framework									
Subcomponent 1.1. Improvement and implementation of the regulatory framework									
(i) Regulatory framework									
(a) Report on actions taken to publicize the new State-owned Enterprises Act (LOEP) and OECD guidelines approved.	Report	0	2018	0	0	0	1	1	Certificate of approval, State-owned Enterprise Holding Company (EMCO), and subsequently the entity that replaces it
(b) LOEP regulations drafted	Rules of procedure	0	2018	0	1	0	0	1	Certificate of receipt, MEF
(c) LOEP reforms supervision report implemented and technical regulations drafted	Report	0	2018	0	0	0	2[10]	2	Certificate of receipt, MEF
(d) SOE civil servants and employees trained in OECD corporate governance guidelines and LOEP reforms	Number of staff	0	2018	0	100	50	50	200	List of participants, EMCO and then the entity that replaces it, showing attendance at public awareness-raising events
(ii) Fiscal governance regime									
(a) Report containing the design of the SOE tax collection function in the Internal Revenue Service (SRI)[11] approved	Report	0	2018	0	0	0	1	1	Certificate of approval, SRI
(b) Report containing the institutional design of tax functions and responsibilities in the SOEs[12]	Report	0	2018	0	0	1	0	1	Certificate of Approval, DNEP
(c) Report containing the design of the oil companies' tax regime approved	Report	0	2018	0	1	0	0	1	Certificate of approval, DNEP

[9] Annual outputs.

[10] Guidelines associated with LOEP.

[11] Consulting service includes training for 20 SRI officials on the SOE tax collection function.

[12] Consulting service includes training for 40 SOE employees to fulfill tax responsibilities.

Indicator	Unit of measure	Base-line	Baseline year	2019	2020	2021	2022	Final target	Means of verification
(iii) Transparency and accountability									
(a) SOE employees trained in implementation of International Financial Reporting Standards (IFRS) and financial statement reporting	Employees	0	2018	0	25	20	0	45	List of participants, EMCO and subsequently the entity that replaces it, showing course attendance.
(b) Report containing criteria for the prequalification of external auditors approved	Report	0	2018	0	1	0	0	1	Certificate of approval, DNEP
(c) Report on technical consulting services to support SOE ISO-37001 certification approved	Report	0	2018	0	2	3	0	5	Certificate of approval, EMCO
Subcomponent 1.2. Redesign of the ownership and management functions									
(i) Support for implementation of the SOE holding company to replace EMCO									
(a) Supervision report on measures to implement the new SOE holding company and the administrative charter delivered	Report	0	2018	0	1	0	0	1	Certificate of receipt, EMCO
(b) Employees trained in the functions of the new SOE holding company	Employees	0	2018	0	0	40	0	40	List of participants, EMCO and subsequently the entity that replaces it, showing course attendance.
(c) Report on actions taken to publicize the new SOE holding company	Report	0	2018	0	0	1	0	1	Certificate of approval, EMCO and subsequently the entity that replaces it
(d) Performance management report on the contract between the holding company and SOEs approved [13]	Report	0	2018	0	1	0	0	1	
(ii) Strengthening of the DNEP									
(a) Production cost studies to support budget formulation approved	Study	0	2018	0	1	0	0	1	Certificate of approval, DNEP
(b) Report on the design of payment capacity and debt ceiling certification systems approved.	Report	0	2018	0	1	0	0	1	
(c) Software to produce financial statistics through specialized reporting systems implemented	Software	0	2018	0	0	1	0	1	Verification of use by at least one user, DNEP
(d) Staff trained in strategic sectors	Number of staff	0	2018	0	5	5	5	15[14]	List of participants, DNEP

[13] Consulting service includes training for employees of the SOE holding company on the performance management contract.

[14] Oil and gas, electricity, and telecommunications sector.

Indicator	Unit of measure	Base-line	Baseline year	2019	2020	2021	2022	Final target	Means of verification
(iii) Support for decentralized autonomous governments									
(a) Number of decentralized autonomous governments that receive technical assistance to adopt the LOEP reforms in their SOEs.	Decentralized autonomous government	0	2018	0	30	60	60	150	Approval of report containing a list of decentralized autonomous governments receiving assistance, DNEP
(b) Report on financial sustainability analysis of SOEs attached to decentralized autonomous governments approved	Report	0	2018	0	1	0	0	1	Certificate of approval, DNEP. Includes design and implementation
Component 2: SOE portfolio optimization									
Subcomponent 2.1. SOE redesign									
(i) Support for the Petroamazonas-Petroecuador merger									
(a) Report on Petroamazonas-Petroecuador merger strategy approved	Report	0	2018	1	0	0	0	1	Certificate of approval, MERNNR
(b) Reports in support of the Petroamazonas-Petroecuador merger approved	Reports	0	2018	0	3	0	0	3[15]	Certificate of approval, MERNNR The reports are associated with milestones. See the monitoring and evaluation plan.
(c) Report on technical issues in the value chain (oil exploration and production) approved, to enhance efficiency in the merger	Report	0	2018	0	0	1	0	1	Certificate of approval, MERNNR
(d) Management software implemented	Software	0	2018	0	0	1	0	1	Verification of use by at least one user, MERNNR
(e) Legal report on the merger approved	Report	0	2018	0	0	1	0	1	Certificate of approval, MERNNR
(ii) Optimization of CELEC and CNEL operations									
(a) Report on the optimization of CELEC and CNEL operations	Report	0	2018	0	0	1	0	1	Certificate of approval, MERNNR
(iii) Appraisal of TAME assets									
(a) TAME appraisal report approved	Report	0	2018	0	1	0	0	1	Certificate of approval, MTOP
(b) Financial statements observing IFRS 2017-2018 approved	Financial statements	0	2018	1	1	0	0	2	Certificate of approval, TAME. 2017 and 2018 financial statements observing IFRS

[15] According to the preliminary document, the merger is implemented in three phases.

Indicator	Unit of measure	Base-line	Baseline year	2019	2020	2021	2022	Final target	Means of verification
Subcomponent 2.2. Improved management and optimization of human talent									
(i) Petroamazonas, Petroecuador, CNEL, CELEC, TAME, and EMCO staff who benefit from severances.	Number of staff	0	2018	0	3,350	0	0	3,350	Audit reports, DNEP. MERNNR, MTOP, and EMCO will complement the verification of severance payments.
(ii) Annual reports produced on the (public and internal) communication strategy to facilitate understanding of the reform's objectives and benefits to citizens.	Report	0	2018	1	1	1	1	4	Certificate of approval, DNEP

FIDUCIARY AGREEMENTS AND REQUIREMENTS

Country	Ecuador
Project number:	EC-L1251
Name:	Program to Support State-owned Enterprise Reform
Executing agency:	Ministry of Economy and Finance (MEF)
Subexecuting agencies:	State-owned Enterprise Holding Company (EMCO) (or the entity that replaces it), Ministry of Energy and Nonrenewable Natural Resources (MERNNR), Ministry of Transportation and Public Works (MTOP), Petroecuador, Petroamazonas, Corporación Eléctrica del Ecuador (CELEC), Corporación Nacional de Electricidad (CNEL), and the Ecuadorian National Airline (TAME)
Prepared by:	Carolina Escudero and Juan Carlos Dugand (FMP/CEC)

I. SUMMARY

1.1 The fiduciary agreements for the program's procurement and financial management take account of the following: (i) the country's fiduciary context; (ii) the fiduciary risk assessment; (iii) activities to supervise execution of the loans for which the MEF is responsible; (iv) assessment of the MEF's institutional capacity; and (v) inputs from meetings held with teams and entities involved in project execution.

II. THE COUNTRY'S FIDUCIARY CONTEXT

2.1 **Country procurement system.** Based on document GN-2680-2, which was approved by the Bank's Board of Executive Directors on 13 May 2014, the MEF signed the "Initial Agreement for use of the SNCP of Ecuador in IDB-financed projects" with the National Public Procurement Service of Ecuador (SERCOP) and the Bank. Paragraph 3.2 of the Initial Agreement envisages the National Public Procurement System (SNCP) being applied in seven projects, before being gradually expanded. The Initial Agreement was concluded on 31 December 2018; an evaluation of its functioning is currently under way, and a new agreement on the use of SNCP will subsequently be prepared and signed.

2.2 **Financial management system.** Central government entities use the online financial management system (e-SIGEF), which integrates budget, accounting, and cash management processes. Government entities are subject to control and oversight by the Office of the Comptroller General (CGE). In general, Ecuador's country financial management systems have an adequate level of development, although they need to be supplemented to execute Bank-financed projects, in terms of financial reporting with nonaccounting records and external audits by firms acceptable to the Bank. The government plans to replace e-SIGEF with a new system in 2020.

III. THE EXECUTING AGENCY'S FIDUCIARY CONTEXT

3.1 The program's executing agency is the MEF, acting through the National State-owned Enterprise Directorate (DNEP); and the subexecuting agencies will be the ministries to which the beneficiary State-owned enterprises (SOEs) are attached, and the SOEs themselves in relation to severance payments. The MEF has previously served as the executing agency of Bank-financed programs that have similar arrangements in which several State entities participate; and its role of coordination, centralization, and support to the subexecuting agencies is fundamental for maintaining the program's integrity. The ministry has recently executed loans 3073/OC-EC, 3726/OC-EC, 4614/OC-EC, 4670/OC-EC, and 4364/OC-EC.

3.2 The MEF's DNEP will need to hire staff with experience in programs funded by multilateral agencies, for the issues of procurement, financial management, planning, and monitoring to support the work of the MEF as executing agency, and the work of the subexecuting agencies.

3.3 The ministries will make the contracts and payments needed to undertake the activities envisaged for each of their SOEs, except for staff severance payments, which will be paid for directly by the SOEs themselves, using funds previously assigned by the MEF.

3.4 For procurement and record-keeping, the MEF and the subexecuting agencies use the country systems hosted on the SERCOP portal. For financial management, the MEF and the ministries use the national e-SIGEF system, while the SOEs use their own systems. Both the MEF and the subexecuting agencies have internal control units and are subject to external control by the CGE.

IV. FIDUCIARY RISK EVALUATION AND MITIGATION ACTIONS

4.1 The following medium-high fiduciary risks were identified: (i) delays in program implementation due to insufficient technical staff at the executing agencies, owing to high turnover rates, compounded by a lack of staff with experience in implementing programs with multilateral agencies. As a mitigation measure, the MEF team needs to be reinforced with the following, at least: a program coordinator, a financial specialist, a procurement specialist, and a planning and monitoring specialist, to serve from the start of execution through to loan closure; and (ii) difficulties in monitoring the funds disbursed to the different executing units and delays in program implementation owing to participation by multiple entities, some of which are outside the central government domain. As a mitigation measure, the execution mechanism calls for the MEF to coordinate and centralize all information; contracting and payments pertaining to activities that benefit the SOEs to be handled by the line ministries, which are part of central government; and SOE staff severance payments to be made through reimbursements rather than advances of funds.

V. AGREEMENTS AND REQUIREMENTS FOR PROCUREMENT EXECUTION

5.1 **Procurement execution.** The MEF will update the procurement plan annually at least, through the Procurement Plans Management System (SEPA). The program's main procurements are listed in Table 2.

5.2 **Procurement of works, goods, and nonconsulting services:** These processes will use the Bank's standard bidding documents, applying any of the methods described in the respective policies (version GN-2349-9 or later).[1] Table 1 displays the procurement thresholds.

5.3 **Selection and contracting of consultants (firms):** These processes will use the Bank's standard request for proposals, applying any of the methods described in the respective policies (version GN-2350-9 or later).[2] Table 1 indicates the threshold above which shortlists must include international consultants.[3]

5.4 **Selection of individual consultants:** These processes will abide by Section V of the policies for contracting consultants.

5.5 **Use of the country procurement system:** The SNCP will be implemented pursuant to the New Agreement on Use of the SNCP mentioned in paragraph 2.1.

5.6 **Advance procurement and retroactive financing**: The Bank may provide retroactive financing, as a charge against the loan proceeds, of up to US$15 million (20% of the loan amount) for eligible expenditures incurred by the borrower prior to the loan approval date, in order to engage the consulting services needed to prepare conceptual designs, to establish the execution units, and to cover priority layoffs that are already under way and that being financed with government funds, provided that all such expenditures have met requirements substantially similar to those specified in the loan contract. Expenditures must have been incurred on or after the project profile approval date of 15 February 2019, but under no circumstances may they have been incurred more than 18 months prior to the loan approval date.

5.7 **National preference**: In contracts subject to international competitive bidding (ICB), bids to supply goods originating in the borrower's country will benefit from a 15% price preference.[4]

Table 1. Table of thresholds

Works			Goods			Consulting	
ICB	National competitive bidding (NCB)	Shopping	ICB	NCB	Shopping	International advertising for consulting services	100% national shortlist
≥ US$3 million	< US$3 million ≥ US$250,000	< US$250,000	≥ US$250,000	< US$250,000 ≥ US$50,000	< US$50,000	≥ US$200,000	< US$200,000

1 Under the Bank's procurement policies (document GN-2349-9), nonconsulting services are treated as goods.
2 Pursuant to the Bank's policies on contracting consultants (document GN-2350-9).
3 In contracts for less than US$200,000, the shortlist may consist exclusively of national consulting firms.
4 Pursuant to Appendix II of the Bank's procurement policies (document GN-2349-9) and the loan contract.

Table 2. Main procurement items

Procurement item	Selection method	Estimated date of invitation	Estimated amount (US$000)
Consulting services (firms)			
Specialized consulting service to design the Petroamazonas-Petroecuador merger strategy, including definition of corporate governance and tax regime.	Quality- and cost-based selection (QCBS)	Q4-2019	10,000
Specialized consulting service to implement the Petroamazonas-Petroecuador merger strategy, including definition of corporate governance and tax regime.		Q4-2019	8,000
Specialized consulting service to optimize CELEC and CNEL operations, including: (a) an institutional diagnostic assessment of both entities and a coordinated proposal for management of the electric power sector; (b) implementation of the LOEP reforms; (c) production cost studies, including estimation of asset value and operating costs.		Q4-2019	3,000
Specialized consulting service for institutional design of the SOE tax collection function of the Internal Revenue Service (SRI), including training on this for SRI civil servants.		Q2-2020	488
Five specialized consulting service contracts to support the implementation of anticorruption measures (obtaining ISO-37001 SOE certification) for PAM, PEC, CELEC, CNEL, CNT, and FLOPEC.		Q4-2020	1,150
Specialized consulting service to design the corporate governance strategy and tax regime of TAME (asset valuation).		Q4-2019	500
Specialized consulting service to optimize CNT operations.		Q4-2020	500
Specialized consulting service to implement the public and internal communication strategy to facilitate understanding of the reform's objectives and the strategies designed to benefit citizens, including public awareness-raising events.		Q4-2019	555
Goods and nonconsulting services			
10 contracts for activities of awareness raising, dissemination, and training on the new regulations, standards, and implementation.	NCB/Shopping	From Q3/2020	708
Individual consulting services			
5 professionals to serve as operational coordinator, financial specialist, procurement specialist, planning and monitoring specialist, and execution support during the four years of program execution.	National individual consultant selection based on qualifications (NICQ) / International individual consultant selection based on qualifications (IICQ)	Q4-2019	855
4 professionals to provide sector-specific technical consulting during the four years of program execution: 1 legal specialist, 1 oil and gas specialist, 1 energy specialist, and 1 telecommunications specialist.		Q4-2019	591
2 specialists to provide specialized consulting services to support implementation of the LOEP reforms, including the definition of systems for the selection of directors, per-diem policies, and instruments for measuring the SOE's performance.		Q3-2020	396
2 specialists to provide specialized consulting services to monitor implementation of the design of the new SOE holding entity that will replace EMCO, including preparation of the respective administrative charter.		Q4-2019	208
2 specialists to provide specialized consulting services to develop management tools (production cost studies) to assist budget formulation.		Q2-2020	218
4 specialists to provide specialized consulting services to support the process of implementing the new SOE management model.		Q4-2020	306

The itemized procurement plan can be accessed here.

5.8 **Procurement supervision.** The procurement plan will indicate the supervision method to be used by the Bank. Ex post reviews will be conducted annually as indicated in Appendix 1 of the policies, and will include physical inspections where the Bank sees fit.

Table 3. Ex post review thresholds

Works	Goods	Consulting services	Individual consultants
< US$3 million	< US$250,000	< US$200,000	< US$50,000

Note: Amounts set on the basis of the executing agency's fiduciary capacity for execution, which can be adjusted in the event of variations.

5.9 **Records and files**. The executing agency will keep all files in a complete and orderly manner, organized chronologically, independently, and by process and financing source.

VI. Financial Management Agreements and Requirements

6.1 **Programming and budget.** The Basic Code of Planning and Public Finance (COPYFP) specifies the rules governing budget programming, formulation, approval, execution, control, evaluation, and liquidation. These rules are applied to the implementation of programs financed by the Bank in Ecuador. Both e-SIGEF and the new system to be developed by the government instrumentalize and standardize application of these norms throughout national public administration. The MEF will take steps to incorporate and/or update the investment program as necessary, with a view to securing the respective budgetary appropriations.

6.2 In the case of the severance packages that will be processed, the SOEs' budgets must include the income and payments to be made, with authorization from their boards of directors.

6.3 **Accounting and information systems.** Project accounts will be kept in e-SIGEF, or the system that replaces it; and all program commitments and payments will be recorded there. Nonaccounting records, including the payments made by the SOEs themselves, will be needed to generate the program's financial reports.

6.4 **Disbursements and cash flow.** Since 2008, the Government of Ecuador has used the National Treasury Single Account (TSA) mechanism, which unifies cash management for all central government entities. The SOEs are not included in this account.

6.5 The implementation of this mechanism did not eliminate the system of special accounts, or special-purpose accounts, which the Central Bank of Ecuador (BCE) uses to receive multilateral loan financing. The program will maintain an exclusive account with the BCE, into which the loan funds will be disbursed.

6.6 With the exception of severance payments, all program payments will be executed through e-SIGEF, or the new system that replaces it, through a TSA debit.

6.7 Severance payments will be made by the SOEs themselves using funds previously allocated by the MEF. Subsidiary agreements signed between the MEF and the SOEs will specify the conditions for fund transfer, payment, and reimbursement.

6.8 The Bank will make loan disbursements in the form of advances of funds, to meet the project's real liquidity needs according to the financial plan, except for disbursements in respect of staff severance payments. The Bank may also make direct payments to suppliers or reimburse other expenses at the borrower's request.

6.9 For severance-related disbursements, the Bank will reimburse the payments made, subject to verification by an independent auditing firm, compliance with the legal requirements, and fulfillment of the criteria established in the Program Operating Regulations.

6.10 The MEF will manage program disbursements.

6.11 Supporting documentation for payments will be reviewed by the Bank and/or the external auditors ex post, after the funds have been disbursed.

6.12 **Internal control and internal audit.** The Constitution of the Republic of Ecuador puts the CGE in charge of the public sector oversight system. As part of this sector, the executing agency has its own internal audit area that reports directly to the CGE.

6.13 **External control and reports.** Although the CGE has the authority to audit public sector entities, projects are not necessarily included in the annual audit plan. This project will be audited by an external firm of independent auditors acceptable to the Bank, pursuant to OP-273-6. The firm will be contracted by the MEF under previously agreed-upon terms of reference, and it will be financed out of program funds. During program execution, audited financial reports will be submitted annually, within 120 days following each financial year-end, or, in the case of the final audit, no later than 120 days after the date of the final disbursement.

6.14 As noted in paragraph 6.9, the external audit firm will also verify that the requirements for paying severances have been fulfilled in respect of claims for reimbursement of expenses incurred. The Bank may also request additional unaudited financial reports or project-related reports as it sees fit.

6.15 Although there is no national policy on the public disclosure of audit reports, the Bank's current access to information and disclosure policy requires audited project reports to be published on its website.

Table 4. Supervision plan

<table>
<tr><th rowspan="3">Supervision activity</th><th colspan="4">Supervision plan</th></tr>
<tr><th rowspan="2">Nature and scope</th><th rowspan="2">Frequency</th><th colspan="2">Party responsible</th></tr>
<tr><th>Bank</th><th>Third party</th></tr>
<tr><td rowspan="2">Operational</td><td>Review of progress report</td><td>Semiannual</td><td rowspan="2">Project team</td><td rowspan="2">MEF</td></tr>
<tr><td>Portfolio review</td><td>As agreed with the MEF</td></tr>
<tr><td rowspan="4">Financial</td><td>Review of cash flow programming and disbursement execution</td><td>At the Bank's request, with each application for advance of funds, in portfolio reviews, or during supervision visits</td><td>Project team</td><td rowspan="3">MEF</td></tr>
<tr><td>Supervision visits</td><td>Annual</td><td>Financial Specialist</td></tr>
<tr><td>Review of audited and unaudited financial reports</td><td>Annual</td><td>Project Team Leader and financial specialist</td></tr>
<tr><td>Review of disbursement requests</td><td>Periodic</td><td>Project Team Leader and financial specialist</td><td>MEF / auditors</td></tr>
<tr><td rowspan="3">Procurement</td><td>Ex post review of procurement processes</td><td>According to supervision plan</td><td>Project Team Leader and procurement specialist</td><td>MEF/sub-executing agencies</td></tr>
<tr><td>Ex ante review of procurement processes</td><td>According to the Procurement Plan</td><td>Project Team Leader /AO and procurement specialist</td><td>MEF/sub-executing agencies</td></tr>
<tr><td>Procurement plan update</td><td>Annual</td><td>Project Team Leader and procurement specialist</td><td rowspan="3">MEF</td></tr>
<tr><td rowspan="3">Compliance</td><td>Fulfillment of conditions precedent</td><td>Once only</td><td rowspan="2">Project team</td></tr>
<tr><td>Budget allocation review</td><td>Annual</td></tr>
<tr><td>Submission of audited financial reports</td><td>Annual</td><td>Project Team Leader and financial specialist</td><td>MEF / auditors</td></tr>
</table>

6.16 **Execution mechanism**. The program's executing agency is the MEF, acting through the DNEP. The subexecuting agencies are as follows: (i) EMCO, or the new entity that replaces it; (ii) the MERNNR; (iii) the MTOP; and (iv) Petroecuador, Petroamazonas, CELEC, CNEL, and TAME, for severance payments. See paragraphs 3.1 to 3.10 of the main document and paragraph 3.1 of this one.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-__/19

Ecuador. Loan ____/OC-EC to the Republic of Ecuador
State-owned Enterprise Reform Support Program

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Republic of Ecuador, as borrower, for the purpose of granting it a financing to cooperate in the execution of the State-owned Enterprise Reform Support Program. Such financing will be for the amount of up to US$75,000,000 from the resources of the Bank's Ordinary Capital, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on ___ ___________ 2019)

LEG/SGO/CAN/EZSHARE-263631146-18670
EC-L1251