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R2019-0271/1

November 26, 2019

**Closing Date: Tuesday, December 17, 2019
at 6:00 p.m.**

FROM: Vice President and Corporate Secretary

Sri Lanka - Public Sector Efficiency Strengthening Project

Project Appraisal Document

Attached is the Project Appraisal Document regarding a proposed loan to Sri Lanka for the Public Sector Efficiency Strengthening Project (R2019-0271), which is being processed on an absence-of-objection basis.

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Report No: PAD2903

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROJECT APPRAISAL DOCUMENT
ON A
PROPOSED LOAN

IN THE AMOUNT OF US\$25 MILLION

TO THE

DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

FOR A

PUBLIC SECTOR EFFICIENCY STRENGTHENING PROJECT

November 21, 2019

Governance Global Practice
South Asia Region

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CURRENCY EQUIVALENTS

(Exchange Rate Effective October 1, 2019)

Currency Unit = Sri Lanka Rupee (LKR)
LKR 182 = US\$1

FISCAL YEAR
January 1 — December 31

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ABBREVIATIONS AND ACRONYMS

ADB	Asian Development Bank	NPC	National Procurement Commission
AGD	Attorney General's Department	NPD	National Planning Department
CBSL	Central Bank of Sri Lanka	OC	Operational Committee
CPF	Country Partnership Framework	OGP	Open Government Partnership
DA	Designated Account	PDO	Project Development Objective
DeMPA	Debt Management Performance Assessment	PEFA	Public Expenditure and Financial Accountability
DFAT	Department of Foreign Affairs and Trade	PFM	Public Financial Management
DLI	Disbursement-linked Indicator	PIM	Public Investment Management
DLR	Disbursement-linked Result	PIMA	Public Investment Management Assessment
DoI	Department of Government Information	PIP	Public Investment Plan
DPL	Development Policy Loan	PMU	Project Management Unit
EEP	Eligible Expenditure Program	POM	Project Operations Manual
EU	European Union	PPP	Public Private Partnerships
FM	Financial Management	PPSD	Project Procurement Strategy for Development
GDP	Gross Domestic Product	PSC	Project Steering Committee
GoSL	Government of Sri Lanka	PT	Project Team
GRS	Grievance Redress Service	RTI	Right to Information
IMF	International Monetary Fund	RETF	Recipient Executed Trust Fund
IPF	Investment Project Financing	SAI	Supreme Audit Institution
IRR	Internal Rate of Return	SAI-PMF	Supreme Audit Institution-Performance Measurement Framework
IT	Information Technology	SMEs	Small and Medium Enterprises
IUFR	Interim Unaudited Financial Report	SOEs	State-Owned Enterprises
IVA	Independent Verification Agent	SORT	Systematic Operations Risk-Rating Tool
M&E	Monitoring and Evaluation	TA	Technical Assistance
MfD	Maximizing finance for Development	USAID	United States Agency for International Development
MNPEA	Ministry of National Policies and Economic Affairs		
MoF	Ministry of Finance		
NAOSL	National Audit Office of Sri Lanka		



TABLE OF CONTENTS

DATASHEET	1
I. STRATEGIC CONTEXT	6
A. Country Context.....	6
B. Sectoral and Institutional Context	6
C. Relevance to Higher Level Objectives.....	9
II. PROJECT DESCRIPTION.....	9
A. Project Development Objective (PDO)	9
B. Project Components	10
C. Project Beneficiaries	13
D. Results Chain	14
E. Rationale for Bank Involvement and Role of Partners	14
F. Lessons Learned and Reflected in the Project Design	14
III. IMPLEMENTATION ARRANGEMENTS	16
A. Institutional and Implementation Arrangements	16
B. Results Monitoring and Evaluation Arrangements.....	17
C. Sustainability.....	17
IV. PROJECT APPRAISAL SUMMARY	18
A. Technical, Economic and Financial Analysis (if applicable)	18
B. Fiduciary.....	19
C. Safeguards	20
V. KEY RISKS	22
VI. RESULTS FRAMEWORK AND MONITORING	34
ANNEX 1: Implementation Arrangements and Support Plan	40



DATASHEET

BASIC INFORMATION

Country(ies)	Project Name	
Sri Lanka	Sri Lanka Public Sector Efficiency Strengthening Project	
Project ID	Financing Instrument	Environmental Assessment Category
P162949	Investment Project Financing	C-Not Required

Financing & Implementation Modalities

<input type="checkbox"/> Multiphase Programmatic Approach (MPA)	<input type="checkbox"/> Contingent Emergency Response Component (CERC)
<input type="checkbox"/> Series of Projects (SOP)	<input type="checkbox"/> Fragile State(s)
<input type="checkbox"/> Disbursement-linked Indicators (DLIs)	<input type="checkbox"/> Small State(s)
<input type="checkbox"/> Financial Intermediaries (FI)	<input type="checkbox"/> Fragile within a non-fragile Country
<input type="checkbox"/> Project-Based Guarantee	<input type="checkbox"/> Conflict
<input type="checkbox"/> Deferred Drawdown	<input type="checkbox"/> Responding to Natural or Man-made Disaster
<input type="checkbox"/> Alternate Procurement Arrangements (APA)	

Expected Approval Date	Expected Closing Date
17-Dec-2019	31-Dec-2024

Bank/IFC Collaboration

No

Proposed Development Objective(s)

To improve transparency and the efficiency of core government and public financial management functions.

Components

Component Name	Cost (US\$, millions)
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Strengthening Allocative Efficiency of Public Investments, Programs and Excise Management	21.44
Improving the operational efficiency of and transparency in Public Expenditures through Procurement	14.00
Strengthening the Governance, Transparency and Efficiency of Public Services	6.00
Project management	1.00
Front end fee	0.06

Organizations

Borrower:	Democratic Socialist Republic of Sri Lanka
Implementing Agency:	Ministry of Finance National Audit Office of Sri Lanka

PROJECT FINANCING DATA (US\$, Millions)

SUMMARY

Total Project Cost	42.50
Total Financing	42.50
of which IBRD/IDA	25.00
Financing Gap	0.00

DETAILS

World Bank Group Financing

International Bank for Reconstruction and Development (IBRD)	25.00
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Non-World Bank Group Financing

Counterpart Funding	10.00
Borrower/Recipient	10.00
Other Sources	7.50
EC: European Commission	7.50

Expected Disbursements (in US\$, Millions)



WB Fiscal Year	2020	2021	2022	2023	2024	2025
Annual	3.70	1.30	0.40	6.50	7.80	5.30
Cumulative	3.70	5.00	5.40	11.90	19.70	25.00

INSTITUTIONAL DATA**Practice Area (Lead)**

Governance

Contributing Practice Areas

Macroeconomics, Trade and Investment

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

Gender Tag**Does the project plan to undertake any of the following?**

a. Analysis to identify Project-relevant gaps between males and females, especially in light of country gaps identified through SCD and CPF	Yes
b. Specific action(s) to address the gender gaps identified in (a) and/or to improve women or men's empowerment	Yes
c. Include Indicators in results framework to monitor outcomes from actions identified in (b)	Yes

SYSTEMATIC OPERATIONS RISK-RATING TOOL (SORT)**Risk Category****Rating**

1. Political and Governance	● Substantial
2. Macroeconomic	● Substantial
3. Sector Strategies and Policies	● Moderate
4. Technical Design of Project or Program	● Moderate
5. Institutional Capacity for Implementation and Sustainability	● Substantial
6. Fiduciary	● Moderate
7. Environment and Social	● Low



8. Stakeholders	● Moderate
9. Other	
10. Overall	● Substantial

COMPLIANCE

Policy

Does the project depart from the CPF in content or in other significant respects?

☐ Yes ☒ No

Does the project require any waivers of Bank policies?

☐ Yes ☒ No

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01		✓
Performance Standards for Private Sector Activities OP/BP 4.03		✓
Natural Habitats OP/BP 4.04		✓
Forests OP/BP 4.36		✓
Pest Management OP 4.09		✓
Physical Cultural Resources OP/BP 4.11		✓
Indigenous Peoples OP/BP 4.10		✓
Involuntary Resettlement OP/BP 4.12		✓
Safety of Dams OP/BP 4.37		✓
Projects on International Waterways OP/BP 7.50		✓
Projects in Disputed Areas OP/BP 7.60		✓

Legal Covenants

Sections and Description

1. By no later than six months after the Effective Date, the Borrower shall establish, and thereafter maintain, throughout the implementation of the Project, a Project Steering Committee within its MoF, with attributions, composition and organization acceptable to the Bank, which shall be: (a) chaired by the Secretary to the Treasury or his/her representative and shall include high level representatives of all ministries, departments and



independent commissions involved in the Project; and (b) provide strategic guidance on Project activities, oversight for Project implementation, ensure effective inter-agency coordination and communication, and mandate remedial action as appropriate. (Section I.A.1 of Schedule 2 to the Loan Agreement)

Sections and Description

2. By no later than six months after the Effective Date, the Borrower shall establish, and thereafter maintain, throughout the implementation of the Project, a Project Management Unit within its MoF, which: (a) shall be headed by a Project director and include the following key positions: a Project coordinator; a financial management specialist; a procurement officer; and a monitoring and evaluation officer; and (b) inter alia: oversee the implementation of the Project activities, carry out day-to-day overall Project coordination, ensure centralized procurement and provide procurement support; ensure budget and fund availability and supervise financial management, monitor and evaluate the Project's performance, and manage the Project-level grievance and complaints procedures pursuant to the Project Operations Manual. (Section I.A.2 of Schedule 2 to the Loan Agreement)

Sections and Description

3. By not later than six months after the Effective Date, the Borrower shall prepare and adopt a Project Operations Manual as accepted by the Bank, and thereafter ensure that the Project is carried out in accordance with the Project Operations Manual. (Section I.B of Schedule 2 to the Loan Agreement)

Sections and Description

4. For the purposes of carrying out Part 3.2 of the Project, the Borrower, through its NAOSL, shall establish, and thereafter maintain, throughout the implementation of the Project, a NAOSL Project Team with members in adequate number, each with terms of reference, qualifications and experience satisfactory to the Bank.

Conditions

Type	Description
Disbursement	No withdrawal shall be made for EEPs claimed in interim unaudited financial reports under Category (1), unless and until the Borrower has furnished to the Bank evidence, including the relevant Verification Report(s) from the Verification Agent in form and substance satisfactory to the Bank, that the DLR with respect to which withdrawal has been requested has been fully achieved in accordance with the Verification Protocol.



I. STRATEGIC CONTEXT

A. Country Context

1. **Sri Lanka has shown steady growth over the last decade although key macroeconomic challenges persist.** Sri Lanka is a middle-income country with a Gross Domestic Product (GDP) per capita of US\$4,102 (2018) and a total population of 21.7 million people. Following 30 years of civil war that ended in 2009, Sri Lanka's economy grew at an average 5.6 percent during the period of 2010-2018, reflecting a peace dividend and a determined policy thrust towards reconstruction and growth; although growth slowed down in the last few years. The economy is transitioning from a predominantly rural-based economy towards a more urbanized economy oriented around manufacturing and services. Social indicators rank among the highest in South Asia and compare favorably with those in middle-income countries. Economic growth has translated into shared prosperity with the national poverty headcount ratio declining from 15.3 percent in 2006/07 to 4.1 percent in 2016. Extreme poverty is rare and concentrated in some geographical pockets; however, a relatively large share of the population subsists on slightly more than the poverty line. Low fiscal revenues combined with largely non-discretionary expenditure in salary bill, transfers, and interest payments have constrained critical development spending on health, education and social protection, which is low compared to peer countries. Public debt levels are high while the overall debt portfolio indicate some important challenges. The economic outlook is more uncertain following the terrorist attacks of April 2019, though it is too early to assess the economic impact.

2. **The Government's "Vision 2025" policy statement lays out a strategy to foster sustainable and inclusive economic and social development and to substantially increase prosperity for all Sri Lankans.**¹ The Vision aims to make Sri Lanka an Upper Middle-Income Country, a social market economy and a knowledge and logistics hub for South Asia. To achieve these objectives, the Government has initiated a reform program of revenue-based fiscal consolidation, towards a stronger macro-fiscal framework, and a more export-oriented and private sector-led growth model. These reforms seek to address the fiscal and efficiency challenges constraining growth: low and inequitable tax revenues; insufficient productive investments; allocative inefficiencies; budget deficits; and public debt crowding out much needed development expenditures and private sector financing. "Vision 2025" reiterates the Government's commitment to open and inclusive governance based on the principles of public sector transparency and accountability.

B. Sectoral and Institutional Context

3. **Government is committed to fiscal consolidation under a program supported by the International Monetary Fund (IMF)**². Sri Lanka achieved primary surpluses in the fiscal accounts in 2017 and 2018 after many decades but high interest costs continue to mask the overall improvement. Amid slow growth and currency depreciation, the central government debt increased to 84 percent of GDP in 2018. Large foreign currency refinancing requirements – US\$5.5 to US\$6.0 billion annually, starting from 2019 – and the large volume of debt by State-Owned Enterprises (SOEs) and non-commercial state agencies (such as the Road Development Authority), now estimated at 12 percent of GDP, are important fiscal risks. The Government has started to address these risks by passing the Active Liability Management

¹ https://news.lk/images/pdf/2017/sep/Vision_2025_English_final.pdf

² The US\$1.5 billion Extended Fund Facility for Sri Lanka from 2016 to 2019, extended by 1 year to 2020 during the last program review in Sept 2019.



Act in 2018 and by adopting a Medium-Term Debt Management Strategy balancing cost and risks of public debt in 2018. The Government aims to better control the fiscal costs and risks of SOEs through enhanced oversight and performance monitoring of SOEs, including through Statements of Corporate Intent and more stringent vetting of the business case of their investments and State guarantees.

4. **Weak tax revenues at just 10.1 percent GDP in 2014 have hampered the implementation of a strategic fiscal policy and constrained financing for productive development and infrastructure investments.** In response, the Government initiated important tax policy reforms, increasing the rate and eliminating exemptions under the Value Added Tax and the Inland Revenue Act, supported by the IMF. These policies reversed the declining trend and increased tax revenues to 12.5 percent of GDP in 2017. Further reforms are needed if Government is to reach the target of 16 percent of GDP tax revenues by 2025. The Government has launched the second phase of tax reforms which seek to improve the business environment by simplifying tax procedures and compliance – Sri Lanka ranked 141th out of 190 countries on the Paying Taxes indicators in the 2019 Doing Business. Reforms include the modernization of excise policies and administration to increase revenues while also improving public health by making alcohol and tobacco products more expensive.

5. **The Government will address constraints in public investment management (PIM) through a comprehensive public investment management reform.** The recent Public Investment Management (PIM) assessment in Sri Lanka estimated an efficiency gap of 36 percent compared to countries achieving higher infrastructure quality with a similar per capita capital stock and highlighted effectiveness challenges of the existing PIM institutions reflected, amongst others, in a low capital budget execution rate of just 63 percent in 2016. The Government prepared its first Public Investment Plan (PIP) - 2017-2020 in thirteen years in order to improve prioritization and quality of public investments. This is an important effort in a fiscally constrained environment and warrants a strategic use of public investments as catalysts for private investments and leveraging public private partnerships (PPP). The next step is the development of the legal and regulatory framework for the PIM, with rules for project prioritization, appraisal, vetting and selection, supported by an information system for planning and monitoring. These regulations will integrate climate change vulnerability and disaster risk management screening.

6. **While Sri Lanka has a relatively sound Public Financial Management (PFM) system and processes, these can be further strengthened to enhance its performance and the efficiency of its public programs and services in a fiscally constrained environment.** The 2013 Public Expenditure and Financial Accountability (PEFA) assessment³ identified the following strengths of the PFM system: the budget preparation process, given its orderliness which ensures adequate time for preparation, legislative scrutiny and approval; relatively high-quality financial information in the annual financial statements; and timely audit of the country's annual financial statements. It also identified opportunities to improve the PFM system in the areas of budget comprehensiveness and transparency – Sri Lanka ranked 60th among 115 countries on the 2017 Open Budget Index with a score of 44 – budget credibility and predictability budget execution. The Government aims to address these weaknesses through an overhaul of its 1975 public financial management regulations, its information systems and processes. A Public Financial Management Bill that has been approved by the Cabinet and sent to the legal draftsman for finalization and submission to the Parliament. The Bill seeks to modernize public financial management and strengthen budget and public investment management as well as the oversight and accountability of SOEs and agencies. A new Integrated Treasury Management Information System, developed with support from

³ The Sri Lanka PEFA was completed in January 2013 but not published.



an Asian Development Bank (ADB) financed project, is being rolled out across ministries and spending agencies in a phased manner.

7. **Public procurement in Sri Lanka is a source of delays, adversely affecting the completion and cost of projects and delivery of public services.** Procurement data from Bank funded projects shows a time lag of up to one year between the Invitation for Bids for goods and works and the signing of a contract. The underlying causes of delays are cumbersome and outdated procedures and processes, limited understanding of market approaches and lack of capacity and empowerment among procurement decision makers, causing decisions to be elevated to senior management. In the absence of procurement plans and e-procurement system, the Government misses out on opportunities to aggregate demand to leverage economies of scale or better supplier and contractor performance. These factors impact women-led firms, as it is estimated that women entrepreneurs supply only one percent of this market.⁴ According to reports unequal access to economic opportunities is one of the most prevalent factors that constrain the progress of women⁵. The Government is conscious of these challenges and aims to address them through four broad areas of reform: modernization of procurement regulations; improvement and standardization of professional skills of procurement staff; strengthening oversight by the National Procurement Commission; leveraging technology to introduction of e-procurement and data analytics.

8. **Sri Lanka has put in place the legislative framework for open and inclusive governance but has made modest progress in implementation.** The 19th constitutional amendment introduced the citizen's right to access information, strengthened the governance framework and accountability institutions. These principles have been translated into a Right to Information (RTI) Act, a new Audit Act and a new procurement policy. Accountability institutions have been strengthened with the establishment of independent Information, Procurement and Audit commissions. Sri Lanka joined the Open Government Partnership (OGP) and adopted its first action plan (2016-2018). However, limited progress has been made in the implementation of OGP commitments – 1 out of 23 has been achieved – and online proactive disclosure of information, with 85 percent of ministries' disclosure assessed as moderately unsatisfactory or unsatisfactory.⁶ Reactive disclosure has been uneven across ministries and it is not possible to monitor compliance in the absence of an electronic request tracking system.

9. **The Ministries in charge of finance and planning will need to adapt to respond to the broader reform agenda and the responsibilities as laid out in recent legislation.** The Ministry recognizes the need to respond to the changing context through: greater integration and synergies across departments and reforms; a more open, collaborative and inclusive work culture; a stronger focus on public policy objectives and performance beyond compliance; and automation and integration of financial management information systems, with a greater focus on analytics and delivery of services to citizens and firms and the generation, use and disclosure of program evaluations.

10. **The reform program also impacts the Attorney General's Department (AGD) and the National Audit Office of Sri Lanka (NAOSL).** The National Audit Act of July 2018 established the NAOSL and an Audit Service Commission to independently manage its service and cadre. The transformation of the Auditor

⁴ Harris, S. "Gender-smart procurement – policies for driving change". Chatham House, The Royal Institute of International Affairs. December 2017.

⁵ Wong, Y. N. (2012, November). World Development Report 2012: gender equality and development. In Forum for Development Studies (Vol. 39, No. 3, pp. 435-444). Routledge.

⁶ https://www.rti.gov.lk/images/publications/Online-Proactive-Disclosure-under-the-RTI-Act-in-Sri-Lanka_Final-Report.pdf



General's Department into a modern Supreme Audit Institution (SAI) capable of meeting its constitutional mandate and delivering audits in line with international standards will require sustained investment in institutional strengthening. A detailed five year 'Development Action Plan' has been prepared based on an assessment of the performance of NAOSL using the SAI Performance Measurement Framework (SAI-PMF). The AGD is responsible for legislative drafting and providing legal advice to the executive. Its workload has increased sharply in recent years in line with the reform agenda. AGD has identified its capacity building priorities to meet the enhanced mandate and anticipated demand for legal advice to government.

C. Relevance to Higher Level Objectives

11. **The project is fully aligned with and supports the Government of Sri Lanka (GoSL)'s program of governance reforms.** The project supports the accountability policies and institutions created through the 19th amendment to the Constitution, including the Right to Information and the independent information, procurement and audit commissions. The project supports the Government's Vision 2025 which seeks to strengthen public finances, mobilize and allocate resources in line with socio-economic development objectives. The project also supports the implementation of reforms announced in the 2019 budget notably the excise and e-procurement reforms.

12. **The project is aligned with the Country Partnership Framework (CPF) for Sri Lanka for FY17–FY20 as updated by its Performance Learning Review of the CPF FY17-21 No. 135126-LK.** The project will contribute to the achievement of the first CPF pillar on improving macro-fiscal stability and competitiveness. Specifically, it will support the achievement of Objective 1.1: Contributing to improved public finance management as well as Objective 1.2: Improving the enabling environment for private investment and trade. The project will further support the CPF's cross-cutting themes on Governance and on Voice, notably by supporting the implementation of the right to information and citizen engagement reforms. The project builds on the achievements and supports the implementation of key policy reforms initiated under the 2016 Competitiveness, Transparency and Fiscal Sustainability Development Policy Loan (DPL).

II. PROJECT DESCRIPTION

A. Project Development Objective (PDO)

PDO Statement: to improve transparency and the efficiency of core government and public financial management functions.

PDO Level Indicators

The PDO indicators which aim to measure the efficiency and transparency improvements expected from the public financial management and governance reforms supported by the project, are:

1. Share of large projects that are vetted by the new Public Investment Management Committee
2. Enhanced operational efficiency of processes in Excise Management.
3. Reduction in time taken for procurement of standard goods and services and increase in availability of information to the public on contracts approved and awarded at the Cabinet level.



4. Improvement in performance rating of NAOSL in selected priority indicators⁷ as per SAI-PMF assessment.

B. Project Components

13. The US\$25 million Investment Project Financing (IPF), with Disbursement-Linked Indicators, comprises: US\$23 million in results-based financing to provide incentives for achieving results along three components; and US\$2 million in input-based financing for technical assistance (TA) and capacity building to support the GoSL in the implementation of reforms. The project (technical assistance activities) will be supported with a co-financing from European Union (EU). (see para 30 on Role of Partners). The results-based financing will disburse against an Eligible Expenditure Program (EEPs) and incurrence of eligible expenditures, upon achievement of Disbursement-Linked Indicators (DLIs). The Technical Assistance (TA) will disburse against eligible expenditures upon submission of Interim Unaudited Financial Reports (IUFRs).

14. The project has three thematic components and one project management component.

Table 1: Project components and indicative financing (in US\$ million)

Components and sub-components	Project Cost				
	Total	IBRD DLI (1)	GoSL DLI	IBRD TA	EU TA
1. Strengthening Allocative Efficiency of Public Investments, Programs and Excise Management	21.44	13.94	6.00	0.50	1.00
10.69	6.94	3.00	0.25	0.50	
1.1: Strengthening Public Investment Management and Evaluation	10.75	7.00	3.00	0.25	0.50
1.2: Increasing the Efficiency of and Compliance with Excise Taxes					
2. Improving the Operational Efficiency of and transparency in Public Expenditures through Procurement	14.00	9.00	4.00	0.25	0.75
3. Strengthening the Governance, Transparency and Efficiency of Public Services	6.00	-	-	1.00	5.00
1.50	-	-	0.50	1.00	
3.1: Strengthening the Right to Information	2.25	-	-	0.25	2.00
3.2: Strengthening Accountability and Implementation of the Audit Law	2.25	-	-	0.25	2.00
3.3: Strengthening Capacity and Skills of Core Central Departments and Institutions					
4. Project management	1.00	-	-	0.25	0.75
5. Front end fee	0.06	0.06			
Total Project Financing	42.50	23.00	10.00	2.00	7.50

(1): These amounts are indicative and rounded off. The Eligible Expenditure Program supporting the achievement of DLI's is detailed in table 5 - page 36 of 49)

⁷ Domain B- international Governance and Domain E- Human Resources and Training



Component 1: Strengthening Allocative Efficiency of Public Investments, Programs and Excise Management (US\$21.4 million)

Sub-component 1.1: Strengthening Public Investment Management and Evaluation

15. The project will provide technical assistance and capacity building to strengthen public investment management and evaluation, through supporting, inter alia: (i) the design of an integrated public investment management information system; (ii) the formulation of a legal and regulatory framework for public investment management; (iii) the public investment committee in institutionalizing the horizontal coordination across the central departments involved in public investment management; (iv) the implementation of the national evaluation policy and framework, and citizen feedback; and (v) the development and implementation of a climate screening tool as part of the appraisal of large projects above LKR 1bn⁸ to strengthen their resilience and adaptation to climate change.

16. The subcomponent will also incentivize the implementation of the public investment management framework through DLIs and results that support the development of a Public Investment Management system and database for project submission, processing and monitoring, including geotagging of selected projects covering both national and provincial governments. This reform aims to strengthen the vetting and prioritization of high impact projects, enhance transparency and citizen engagement, including in project monitoring.

DLI #1- Public Investment Management		US\$ mn
Strengthened public investment management, efficiency and transparency	The Cabinet has: (i) approved the establishment of the public investment management committee; and (ii) approved and publicly disclosed the guidelines including climate disaster risk screening (Year 1)	1.44
	Public investment management system is operational and includes geotagging of projects for citizen feedback (Year 3)	3.50
	80 percent of Large Investments submitted to National Planning Department (NPD) for review and /or approval have an independent pre-feasibility review published along with the project proposal on the	2.00
Total		6.94

Sub-component 1.2: Increasing the Efficiency of and Compliance with Excise Taxes

17. This sub-component will provide technical assistance and capacity building to increase the efficiency of and compliance with excise taxes, through support for, inter alia: (i) the review and consolidation of excise regulations; (ii) Business Process Review to identify simplification of the procedures and processes of the Department of Excise; (iii) the design of an excise management information system; and (iv) the development and implementation of a training and communication program.

18. The project will incentivize the modernization of excise administration and risk-based controls through DLIs that support: the review of excise regulations and their simplification including by consolidating relevant notifications issued from time to time and the development and the implementation of a web-based Excise information management system, which will enable the online

⁸ As per Circular No MNPEA 2/2019 on public investment guidelines



application, processing and issuance of liquor licenses and permits as well as the online payment of excise taxes and fees. It will be complemented with an online Excise control module to be rolled out to the main alcohol producers, thereby enabling the ease of doing business with improved service standards and a potential phased transition to a risk-based control system for select licensees.

DLI #2 – Excises		US\$ mn
Increased efficiency of excises	Finalization by the Excise Department of the Functional Requirement defining the scope of the excise management system. (Year 1)	1.00
	New excise management system is operational (Year 3)	3.00
	New risk-based excise control system has been rolled out to the largest liquor producer and the largest beer producer in the Borrower's territory	3.00
Total		7.00

Component 2: Improving the Operational Efficiency of and transparency in Public Expenditures through Procurement (US\$14.0 million)

19. The project will support the improvement of procurement outcomes through a combination of results based financing and technical assistance to the Ministry of Finance (MoF) and the National Procurement Commission (NPC). This component will provide technical assistance and capacity building to improve operational efficiency of public expenditures through procurement, by supporting, inter alia: (i) the strengthening of the National Procurement Commission's regulatory and oversight functions; (ii) professionalization of procurement staff through the establishment of standards and skills requirements and a system of accreditation; (iii) the establishment of an independent complaints handling mechanism; (iv) the design of an e-government procurement system; (v) the review and update of the procurement regulations; (vi) an outreach and support pilot program to small and medium enterprises (SMEs) and women entrepreneurs to enhance their access to public tenders in a selected sectors; (vii) the development and pilot testing of a policy and framework for green procurement and more climate resilient infrastructure; and (viii) developing open contracting standards to enhance transparency and accountability;

20. The project will incentivize the development and phased roll out of an e-procurement system through the following DLIs and results.

DLI #3 – Procurement		US\$ mn
e-procurement system operationalized	MoF has finalized the core design of the e-procurement system and officially launched it (Year 1)	2.00
	Procurement plans, and cabinet level tenders and contract awards are published on MoF website (Year 2)	3.00
	The e-procurement system is fully operational and all procuring entities at the central government level are using it (Year 4)	4.00
Total		9.00

Component 3: Strengthening the governance, Transparency and Efficiency of Public Services (US\$6.0 million)

Sub-component 3.1: Strengthening transparency and the Right to Information (RTI)



21. The project will support the implementation of the right to information reform guided by the strategic implementation plans (2017-2020) developed under the Right to Information Act. This sub-component will provide technical assistance and capacity building to The Ministry of Mass Media, the Department of Government Information (DOI) and the Right to Information Commission, by supporting, inter alia: (i) the implementation of selected ministries' right to information mandate; (ii) the proactive disclosure of information on ministries' websites; (iii) the promotion of public awareness and demand for information; and (iv) the strengthening of the Right to Information Commission.

Sub-component 3.2: Strengthening Accountability and the Implementation of the Audit Law

22. This sub-component will provide technical assistance and capacity building support to NAOSL, to: (a) support NAOSL in the implementation of the development action plan; (ii) build institutional and human resource capacities; (iii) enhance capacity for auditing state-owned business enterprises, including by leveraging private auditors; and (iv) develop and pilot test a framework for participatory auditing, that involve the citizens in the audit process.

Sub-component 3.3: Strengthening Capacity and Skills of selected Departments and Institutions

23. This sub-component will provide technical assistance, capacity building and training to the Departments in Treasury and Planning, the Valuation Department, the Attorney General's Department and independent constitutional commissions – including the National Procurement Commission, the Right to Information Commission and the Commission to Investigate Bribery or Corruption. This subcomponent will support these selected departments and institutions: upgrade skills, adapt to reforms and strengthen management capacity. This cross-cutting subcomponent will support capacity building and training activities based on the skills gap and functional training and capacity needs assessment carried out by each agency and a capacity building and training plan validated by the Project Steering Committee (PSC). The process is detailed in Annex 1 and in the project operational manual. This sub-component will be managed by the Project Management Unit (PMU).

Component 4: Project management (US\$1 million)

24. This component will finance the Project Management Unit (PMU), the NAOSL project team, Project Monitoring and Evaluation (M&E) as well as the communications and change management strategy to maximize effectiveness. This component will finance the operating costs of the PMU as well as consultants to support the PMU with the project procurement and fiduciary management.

C. Project Beneficiaries

25. The direct project beneficiaries are the main departments and agencies of the Ministries in charge of finance and of planning, the National Procurement Commission, the Right to Information Commission, the Anti-Corruption Commission, the Attorney-General and NAOSL. The project will also support the implementation of reforms and capacity building in PIM, procurement and RTI in key service delivery ministries.

26. Sri Lankan taxpayers are indirect beneficiaries of the envisaged results of this project in terms of efficiency gains in public investments, expenditures and public procurement. The private sector is expected to benefit from the improved prioritization and implementation of infrastructure investments, more competitive and faster procurement process and from more transparent and simpler Excise licensing. Citizens at large will benefit from increased participation and greater transparency and accountability of the government.



D. Results Chain

27. The chart on Page 10 summarizes the project's results chain and presents the theory of change from the project's inputs and outputs to the expected outcomes required to achieve the development objective.

E. Rationale for Bank Involvement and Role of Partners

28. **The project supports reforms of core government functions which will facilitate private sector investment.** The project facilitates Maximizing finance for Development (MfD) by helping to address upstream governance challenges that constrain private sector investment. Improvements in PIM is expected to catalyze private investments by addressing key institutional bottlenecks to successful investment and identifying public infrastructure that can leverage private sector participation through PPPs or financing. Public procurement reform will foster greater transparency and competition, creating opportunities for a wider range of companies including SMEs. Improved access to information will reduce uncertainty and risk perception for investors.

29. **The project builds on long-standing World Bank policy dialogue and analytical work including through the Competitiveness, Transparency and Fiscal Sustainability DPL.** The Bank is working closely with Sri Lanka's main partners and the project complements activities financed by the IMF, ADB, Department of Foreign Affairs and Trade (DFAT), United States Agency for International Development (USAID) and the EU. The project interventions reflect the support being provided or envisaged by other partners and complements to avoid any overlaps or duplication of efforts.

30. **Role of Partners:** The EU has signed a financing agreement with the Government for Euro 10 million, committing its support to "Strengthening Public Financial Management and Accountability in Sri Lanka"⁹. Of this an amount of US\$7.5 million equivalent will support the project in the form of a Recipient Executed Trust Fund (RETF) which would finance in parallel the technical assistance, capacity building and project management as detailed in Table 1 above.¹⁰ The Administration Agreement between the Bank and EU and the RETF between the Bank and Government have not yet been signed.¹¹

F. Lessons Learned and Reflected in the Project Design

31. **The project design is informed by substantive policy dialogue, global expertise and country specific analytical work.** This includes prior and on-going Bank technical assistance in the areas of public investment management, debt management, excise reform, public financial management, public procurement, Right to Information, external audit and governance of State-Owned Enterprises (See Table 2 on Page 16).

⁹ The EU has signed a financing agreement with the Government for Euro 10 million on May 16, 2018 committing its support to the technical assistance and capacity building with proposed indirect management by the Bank,

¹⁰ A Bank executed trust fund to be funded by the EU in the amount of US\$3.2 million equivalent will be utilized for providing implementation support and analytical and technical support. This trust fund is not part of the project and the achievement of the PDO doesn't depend on activities under the Bank executed Trust fund. See para 50 annex 1 of the PAD.

¹¹ In case the above agreements for the RETF are not signed as intended, it could impact the PDO and the project may require restructuring.

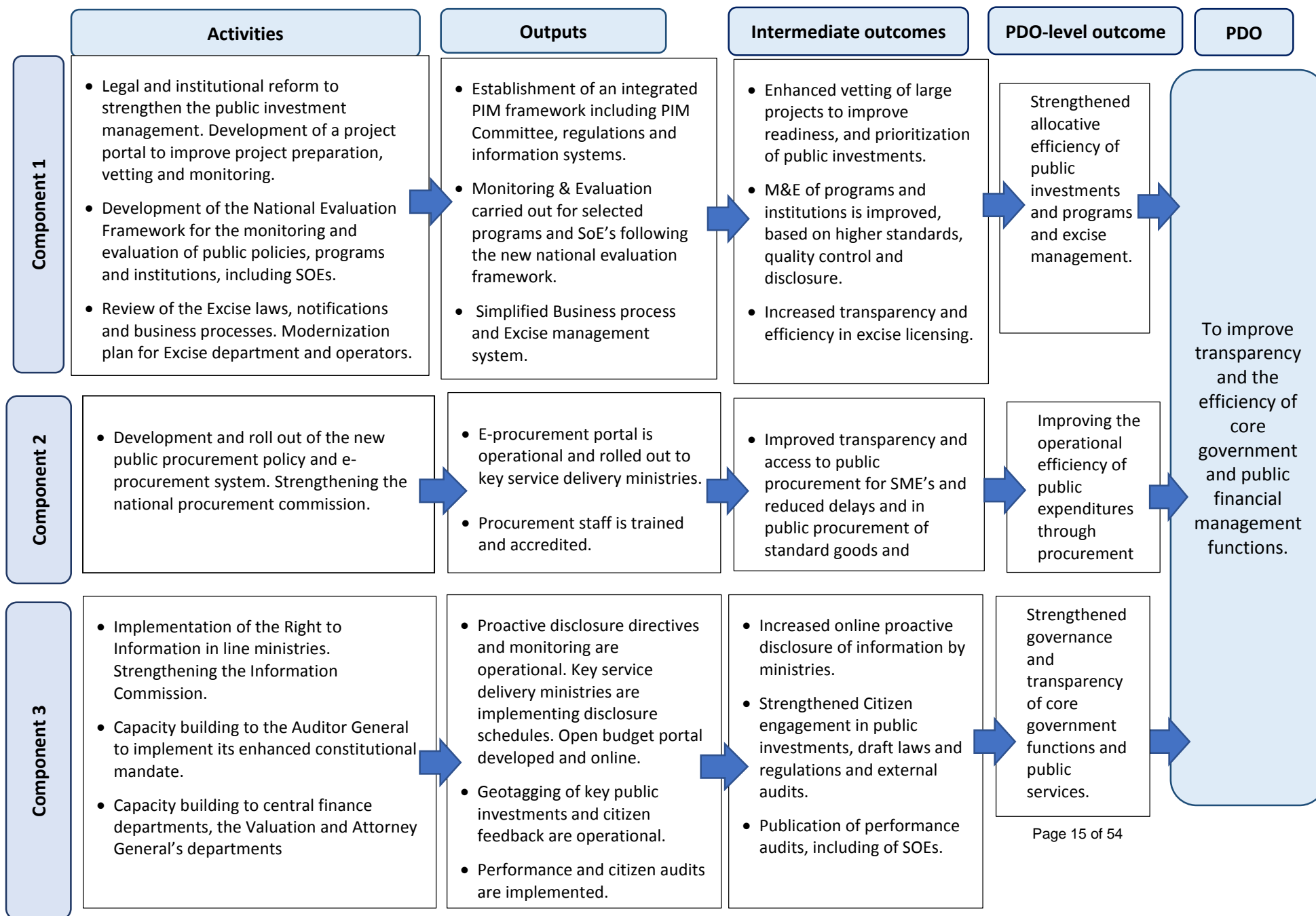




Table 2: World Bank Analytical Work

Component	Analytical work
1	<ul style="list-style-type: none"> • Sri Lanka Public Investment Management Assessment (PIMA)(IMF-WB, 2018); • Country Portfolio Performance Report (WB, 2017 and 2018) • Debt Management Performance Assessment (DeMPA) (WB, 2016) • Excise Policy review and Benchmarking (WB,2018)
2	<ul style="list-style-type: none"> • E-Procurement readiness assessment (USAID, 2017) • PFM Bill technical assistance (WB, 2017-2018) • IT Governance and Institutional assessment (WB, 2018) • PEFA (WB, 2013)
3	<ul style="list-style-type: none"> • Online proactive disclosure of information monitoring framework and assessment (WB-Verite, 2017) • Auditor-General Performance Management Framework Assessment (EU-WB, 2018)
Overall	<ul style="list-style-type: none"> • Sri Lanka Gender gap assessment and action plan (WB, 2017) • Sri Lanka Citizen engagement assessment and roadmap (WB, 2018) • Climate co-benefit assessment (WB 2018)

32. **The project design integrates the lessons learned from past public-sector engagement in Sri Lanka.** It builds on the outcomes and lessons learned from the *Legal and Judicial Infrastructure and Development Project* (P104792), which supported the infrastructure and capacity building of the Attorney General and the Auditor General's Department, taking into account their expanded mandates and functions. The project complements the *Competitiveness, Transparency and Fiscal Sustainability DPL* (P157804), which supported the initial legal reforms of the public finance, audit and RTI acts. These operations highlighted: the benefits of combining results-based financing incentivizing reform implementation and champions, with technical assistance and capacity building to strengthen their sustainability; the need for substantial implementation support through technical assistance and capacity building to achieve the expected results over the medium term; and the need for a communication and change management strategy to address potential resistance to change, promote changes in behavior and organizational culture.

III. IMPLEMENTATION ARRANGEMENTS

A. Institutional and Implementation Arrangements

33. **A Project Steering Committee (PSC) will be established within six months of Effectiveness, to oversee project implementation.** The PSC, chaired by the Secretary to the Treasury or his representative and comprising the Secretaries or Additional Secretaries of the Ministries involved, the head of the treasury departments involved in the project, the Project Director and the heads of the independent institutions involved in the project, will: provide strategic guidance on project activities and oversight for project implementation and its' progress; ensure effective coordination and communication among the project stakeholders; provide directions and mandate remedial action as appropriate.

34. **An Operational Committee (OC), will support the PSC, meet every quarter or more, and provide technical guidance and ensure inter-agency coordination for project implementation at the operational**



level. It thereby complements the Steering Committee Meeting, which provides more higher level strategic direction to the project at least once a year. The OC will be set up in the MoF and chaired by the project director. The OC will include the focal points for each component, including the independent commissions supported by the project as well as the Director-Generals of the Departments participating in the project. The Project Management Unit will serve as the permanent secretariat of the OC.

35. A Project Management Unit (PMU) will be set up under the Ministry of Finance, within six months of Effectiveness. The PMU will be led by a Project Director and will be responsible for the day to day project management, coordination and planning of project activities as well as for the fiduciary, procurement and M&E functions. The PMU will: oversee and support the implementation; undertake centralized procurement and financial management; coordinate project activities, including through the quarterly meetings of the operational committee, chaired by the project director; monitor and evaluate project performance and report on progress; and manage the project-level grievance and complaints procedures pursuant to the Project Operations Manual (POM).

36. Each agency and Independent Commission benefiting from the project will designate officials to a core project team (PT) for the implementation of their respective activities. These commissions include the RTI commission of Sri Lanka, the National Procurement Commission of Sri Lanka, both established under the 19th constitutional amendment. The agencies participating in the project include the Excise department, the Valuation department, the AGD and the NAOSL. The core project team will be responsible for: managing and implementing their respective project sub-components and activities; initiating procurement and providing technical inputs on procurement to be carried out by the PMU, manage the respective contracts, monitor and report on implementation progress and results. NAOSL will directly implement its component and will establish and maintain throughout the implementation of the Project, a PT with members in adequate number, each with terms of reference, qualifications and experience satisfactory to the Bank (“NAOSL Project Team”). The NAOSL Project Team shall, inter alia manage and implement Project activities, provide periodic reports to the PMU and carry out financial management and procurement, all pursuant to the POM. The project implementation arrangements and the mandates and interactions of these governance structures are specified in Annex 1 and the Project Operations Manual.

B. Results Monitoring and Evaluation Arrangements

37. The project M&E framework will track inputs, outputs, and outcomes of the project components. The PMU will hire a Monitoring & Evaluation (M&E) specialist and establish standard formats with baseline information, data, and guidelines for data collection and report updates of M&E to the PSC and the World Bank through the PMU. The PMU will be responsible for monitoring and coordinating this process and may recruit third-party firms as part of the M&E activities to verify the achievement of the DLIs and conduct satisfaction surveys, where relevant.

38. A mid-term review of the project will be carried out within two years of project effectiveness, jointly with the EU. It will assess the project’s ability to achieve the PDO as measured by the key performance indicators and progress made toward achieving the DLIs.

C. Sustainability

39. The sustainability of project investments relates primarily to the continuity – and further strengthening – of policies, procedures and practices supported by the project after the termination of project activities. Sustainability is to be ensured by: anchoring the project in the 19th Constitutional



amendment, which strengthened the country's transparency and accountability policies and institutions, including on public procurement, the right to information and the audit service; aligning activities with the Government's Vision 2025 and related policy declarations, including the budget speech; through an integrated approach supporting the required legal and regulatory changes as well as the systems and investments in the capacity building for those officials carrying out reforms; through a combination of results-based financing creating incentives for time-bound reform implementation and capacity building activities to create incentives for implementation; and by focusing on those areas that offer the greatest potential for efficiency gains to ensure a positive return on investment, detailed in the project's economic and financial analysis below.

IV. PROJECT APPRAISAL SUMMARY

A. Technical, Economic and Financial Analysis (if applicable)

40. **The project design is based on extensive analytical work and policy dialogue in the areas of public investment management, public financial management, public procurement, the right to information, and audit.** The project follows an evidence-based approach to reform implementation using diagnostics to identify the main issues and potential actions, while building consensus on the way forward. The project design process was iterative and participatory, including a stakeholder workshop to discuss in detail all project components, activities and DLIs. It integrates, where relevant, international good practices and standards such as PIMA, DeMPA, SAI-PMF, while taking into account the local context and political economy. The project follows an integrated approach focuses on those areas with the potentially greatest efficiency gains, such as public investment and public procurement. The design follows a sequenced approach starting with the foundations before scaling up and including quick wins to build momentum.

41. **The project design takes into account the political economy context for structural reforms.** The project prioritizes reforms with the strongest commitment and a clear champion: notably PIM, Excise, Procurement, Audit and RTI. The project focuses on core government functions such as PIM, procurement, and supporting the establishment of operational arrangements, such as the thematic committees, that foster cooperation and help overcome institutional fragmentation issues (PIM Committee, Excise Committee, Procurement Working Group, including the National Procurement Commission). The use of DLIs creates incentives for reform implementation and focuses attention on results. The project provides capacity building and technical assistance to the main reform stakeholders and supports change management strategies aimed at building coalitions for reforms, including non-state actors (Civil Society Organizations, private sector for procurement and PIM). Activities include targeted outreach and communication campaigns, leveraging RTI and Citizens engagement and support for the empowerment of reform agents.

42. **The World Bank's value added and comparative advantage relative to other development partners arise from is global expertise and in-depth country knowledge and experience in the implementation of complex institutional reforms.** The Bank will leverage its international experience through its global practices and through peer-to-peer knowledge exchanges with relevant middle-income countries.

43. **The project is expected to have a positive financial and economic impact through the improvement of the allocative and operational efficiency of Sri Lanka's public finances.** While it is not



possible to use a formal rate of return analysis, some of the project's benefits can be estimated in terms of efficiency gains expected from the following reforms and project activities. One area of direct financial benefits has an estimated present value of around US\$65 million from: cost savings from the development and roll out of e-procurement supported UNDER component TWO. This is offset against the present value of inputs of around US\$25million financing these reforms (investment in IT applications, staff inputs and technical assistance) and the EU grant focused on technical assistance and capacity building. In addition, important efficiency gains and economic benefits are expected from the project's support to transparency and access to information, public investment management, excise management, external audit and accountability. The economic analysis and expected impact are specified in Annex 1.

B. Fiduciary

(i) Financial Management

44. **Financial management arrangements are considered satisfactory based on the assessment of the main implementing agency, MoF.** The proposed arrangements for the project including planning, budgeting, accounting, internal controls, funds flow, financial reporting and auditing are in line with fiduciary requirements of Operations Policy 10.00. The PMU, set up under MoF, will be responsible for overall Financial Management (FM) co-ordination, monitoring and FM arrangements for the components and activities under the project. The FM risk is rated as 'Moderate'. The principal risk identified currently for the project is the absence of qualified FM staff. To mitigate this risk, MoF has agreed to nominate FM specialists with adequate experience and qualifications. If needed the project can complement the Ministry's FM staff with qualified FM consultants. The National Audit Office of Sri Lanka will handle the implementation of its technical assistance sub-component by delegation from the MOF and its fiduciary arrangements are considered adequate. While expenditure under category 2 will be reimbursed on the actual expenditures, withdrawals under category 1, will be based on verification of the achievement of the DLRs by an Independent Verification Agent (IVA) as appropriate. The detailed FM arrangements are in Annex 1.

45. **The external audit will be carried out by the National Audit Office of Sri Lanka (NAOSL)** except for the sub-component where NAOSL itself is the implementing entity for which the audit will be carried out by the independent auditor appointed for annual entity audit of the NAOSL. The due date for the submission of audit reports to the World Bank will be within six months of the end of the financial year. Currently there are no overdue audit reports under MoF.

(ii) Procurement

46. **Implementation of the technical assistance component will be supported by a procurement plan and procured by the PMU and NAOSL in accordance with the Bank's Procurement Regulations for IPF Borrowers (July 2016) revised November 2017 and August 2018.** Although the procurement activities for the project are centralized at the PMU, this is not expected to be a substantial workload. A Public Procurement Strategy Document (PPSD) that addresses market risks for the procurement and a draft procurement plan for the project have been prepared. Some procurable items included in the EEP are mainly contracts for training and roll out of the e-procurement and other IT systems under the project well as some hardware like servers and other IT related equipment. The terms of reference for the main activities have been prepared. Given the nature and size of the procurements, no major market risks are envisaged. The main procurement risks identified by the assessment are: inadequate procurement capacities; and need for coordinating procurement across various components of the project. This will be mitigated by PMU engaging a dedicated procurement specialist with experience of World Bank



procurement procedures and train existing procurement staff, specifically on fraud and corruption flags, and on addressing complaints; preparation of an annual procurement progress report by the PMU to share with the Bank; and corrective actions to be taken to address deficiencies identified by the Bank post reviews. The project also directly supports the modernization of Sri Lanka's procurement policy and system, through e-procurement. This is expected to have a positive impact on the project's procurement.

C. Safeguards

Environmental Safeguards

47. **The project has been categorized as an Environment Assessment Category C and no specific environmental safeguard policies are triggered as no environmental impacts are attributed to planned project interventions,** which constitute mainly of system strengthening and technical assistance. The project does not involve either direct or indirect financing of any physical interventions that will lead to direct environmental impacts. Procurement limited procurement of electronic equipment (IT peripherals, servers) which could potentially lead to the limited generation of e-waste. Sri Lanka has a comprehensive policy and regulatory framework for the conservation of natural resources and environmental management. The Central Environmental Authority is the key regulatory body that is mandated by the National Environmental Act to implement all regulatory provisions outlined in its statutes. Given that there are no physical investments under the project, no environmental safeguard policies will be triggered.

Social Safeguards

48. **No adverse social impacts are expected under the project and no social safeguards policies are triggered.** The project is expected to generate social benefits by increasing efficiency, transparency and accountability in the public sector. An action plan has been developed with the project stakeholders to mainstream citizen engagement in the project and country systems, including activities to support: geotagging of public investments and local infrastructure to facilitate citizen monitoring and feedback; establishing a credible and independent procurement Complaints Handling Mechanism and a M&E System to strengthen efficiency and transparency of the public procurement system; implementation of the RTI Act through proactive disclosure of information ; and development and pilot testing of a policy for citizen involvement in the participatory audits conducted by the NAOSL. These policy and institutional reforms will contribute to the government's open government commitments and support country systems for citizen engagement, thereby benefiting the entire WB country program. The above-mentioned policies and their respective information systems will enable citizen to provide online feedback, which will be automatically acknowledged and feed into the respective decision-making process. The respective institutions are expected to respond to the feedback received on their websites. The information systems for public investment management and procurement developed with the project support, will include M&E features to be able to measure Citizen engagement more systematically. The participatory auditing introduced by the NAOSL will be subject to a precise protocol detailing the respective roles and responsibilities of civil society participating in the audit teams.

Climate and Disaster Risk Screening and Climate Co-Benefits

49. **The project has been subject to the World Bank's Climate screening and the overall risk rating of the project is considered moderate.** The risk rating to the development outcome of the project is considered low. Sri Lanka is highly vulnerable to the adverse effects of climate change. The most frequently reported disaster events in Sri Lanka are floods, droughts, landslides and storm surge and



cyclones. The average long-term annual disaster losses are estimated at LKR 50 billion which is equivalent to 0.5 percent of GDP or 3 percent of the total government expenditure. The project supports the integration of climate and disaster screening as part of the national project appraisal and selection process (sub-component 1.1). The green procurement policy (sub-component 2.1) will ensure that contracts awarded through e-Procurement system procure goods, services and works including low emission technologies with a reduced environmental impact throughout their life cycle. The vulnerability context and the detailed project response are specified in Annex 1.

Grievance Redress Mechanisms

50. Communities and individuals who believe that they are adversely affected by a World Bank (WB) supported project may submit complaints to existing project-level grievance redress mechanisms or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address project-related concerns. Project-affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. To submit complaints to the World Bank's corporate GRS, please visit www.worldbank.org/grs. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

D. Gender

51. The project design and activities are informed by a gender gap analysis including the country gender gap assessment, an analysis of the 2018 budget as well as the recent review of gender budgeting in Sri Lanka¹². Building on this analytical work, the project initiated an assessment (completed in 2019) of women led SMEs and their access to public procurement. The findings showed that current public procurement data is neither centralized nor gender disaggregated. Therefore, as a first step, the project will support the Ministry of Finance to include gender information in the vendor registration for its new e-procurement system. This will establish, for the first time, a reliable baseline of female entrepreneurs' access to public tenders. Secondly, as a pilot program, the project will analyze this baseline data to identify the gender gap in procurement in either the Health, Industries or Agriculture sectors. Based on this information the pilot project will help improve women-owned SMEs' access to information on public procurement by (i) ensuring a public procurement environment where measures are introduced to help reduce challenges for female-owned firms in accessing information on public contracts in the selected sector, which would include improving staff awareness on their ability to better target and engage with women-owned SMEs, (ii) providing women-owned SMEs specific assistance to help them participate better in public procurement markets such as improving women-owned SMEs' awareness and knowledge of public procurement opportunities and requirements. The impact of this pilot program will be measured by a gender disaggregated indicator, generated under the e-procurement system introduced by this project, which will enable the government to measure the number of women owned SMEs registering as vendors. This is included in the following intermediary results indicator "Improve efficiency of procurement function", which has the following target - "E-procurement system core design functionalities are being used by over 70 percent of the procuring entities", since capturing gender

¹² The 2018 UN Women Report (draft) titled "Gender budgeting initiatives in Sri Lanka: Achievements and way forward".



disaggregated data is part of the core design functionality for the e-procurement system. The project will therefore track whether there is any increase in women-owned SMEs registering as vendors in the targeted pilot sectors.

52. Acknowledging that there are currently no female accredited staff in procurement, the project will also seek to address this gender gap by encouraging women's formal accreditation for procurement functions. Actions will include setting up a formal accreditation system and creating an enabling environment through conducting sensitization programs. The impact of this work will be monitored under the indicator "Percentage of accredited Procurement staff who are women". The details of the project gender approach and activities are specified in Annex 1.

V. KEY RISKS

53. **Key risks have been identified and rated in the Systematic Operations Risk-Rating Tool (SORT) presented in the project data sheet.** The overall risk of the project is rated Substantial. The environmental and social risks are rated low in the absence of physical investments.

Systematic Operations Risk-Rating Tool (SORT)	
Risk Category	Rating
1. Political and Governance	Substantial
2. Macroeconomic	Substantial
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project	Moderate
5. Institutional Capacity for Implementation and Sustainability	Substantial
6. Fiduciary	Moderate
7. Environment and Social	Low
8. Stakeholders	Moderate
OVERALL	Substantial

54. **The political and governance risk is considered substantial in view of the possible changes in policy priorities in the period before and arising from elections in 2020.** This risk is mitigated by the fact that the project supports reforms that are mandated by the 19th amendment to the Constitution – notably the strengthening of independent procurement, audit and information commissions – and tax and PFM reforms required to strengthen the macro-fiscal framework which underpins the Vision. These governance reforms are supported by Sri Lanka's main development partners, such as the EU, Japan International Cooperation Agency, IMF, ADB and USAID creating a broad-based coalition for reform.

55. **The macroeconomic risk to the project is substantial.** Sri Lanka faces significant macro-fiscal risks, with a very high level of public debt and contingent liabilities from State owned Enterprises. The cost and risk of public debt has been aggravated by the depreciation of the rupee and the April 2019 terrorist attacks. The project aims to mitigate these risks by strengthening the core public financial management



functions, operational efficiency in excise and operational efficiency of public expenditures, through e-procurement which are expected to contribute to macro-fiscal consolidation efforts.

56. **The institutional capacity for implementation and sustainability risks are substantial because many of the core functions of the MoF, such as public investment management are new and fragmented across numerous departments.** The project will mitigate this risk through its focus on institutional strengthening and capacity building. A functional review and skills need assessment will inform the project's capacity building activities. The project will support legal, regulatory, institutional changes and information systems fostering stronger integration, such as the establishment of a PIM committee. During project implementation, institutional capacity risks will be mitigated by the establishment of a strategic and operational steering committee and a strong Project Management Unit (PMU), with a full-time project director and strong linkages with the respective departments.



Disbursement Linked Indicators and Disbursement Linked Results (DLR)

Disbursement Linked Indicator	Responsible Institutions	Total financing allocated to DLI (\$million)	FY [2019/20] (Year 1)	FY [2020/21] (Year 2)	FY [2021/22] (Year 3)	FY [2022/23] (Year 4)	FY [2023/24] (Year 5)
Component 1: Strengthening allocative efficiency of public investments, programs and excise management							
DLI 1: Strengthened public investment management, efficiency and transparency	Secretary of Ministry in charge of planning		DLR 1.1 The Cabinet has: (i) approved the establishment of the public investment management committee; and (ii) approved and publicly disclosed the guidelines including climate disaster risk screening.		DLR 1.2 Public Investment Management system is operational and includes geotagging of projects for citizen feedback.		DLR 1.3 80 percent of Large Investments submitted to NPD for review and /or approval have an independent pre-feasibility review published along with the project proposal on the NPD's official website.



			DLR Baseline: In 2017 there was no integrated institutional arrangement to review and vet public investments. Guidelines were outdated and did not include climate risks.		DLR Baseline: in 2018 there was no information system for public investment submission and approval.		DLR Baseline: In 2018, there was no systematic pre-feasibility review of Large Projects, nor were they disclosed. Formula: US\$1 million for conducting an independent pre-feasibility review and publishing the review together with the project proposal for 50 percent of Large Investments; beyond 50 percent, US\$500,000 for the review and publication relating to an additional 15 percent of Large Investments, up to a total
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							maximum disbursement of US\$2 million.
		6.937	1.437		3.50		2.00
DLI 2: Increased efficiency of excises	MoF/ Excise Department (ED)		DLR 2.1 Finalization by the excise department of the Functional Requirements defining the scope of the excise management system		DLR 2.2 New excise management system is operational		DLR 2.3 New risk-based excise control system has been rolled out to the largest liquor producer and the largest beer producer in the Borrower's territory
			DLR Baseline: No information management system. All processes are manual and paper based.		DLR Baseline:2018: there was no Excise management information system in place. All processes were manual and paper based.		DLR Baseline: In 2018, excise controls were concurrent, transaction-based and manual. Formula: US\$1.5million for the largest liquor operator and US\$1.5 million for the largest



							beer operator, respectively, adopting the new risk-based excise control system.
		7.00	1.00		3.00		3.00
Component 2: Improving the operational efficiency of and transparency in Public Expenditures through procurement							
DLI 3: E-procurement system operationalized	Ministry of Finance		DLR 3.1 MoF has finalized the core design of the e-procurement system and officially launched it.	DLR 3.2 Procurement plans, and cabinet level tenders and contract awards are published on MoF website		DLR 3.3 The e-procurement system is fully operational and all procuring entities at the central government level using it.	
			DLR Baseline: In 2018 there was no electronic procurement system in the Borrower's territory.	DLR Baseline: In 2018 there was no systematic publication of procurement plans, tenders and contract awards.		DLR Baseline: None Formula: US\$2.5 million for 50 percent of all public procuring entities using the E-Procurement System;	



						beyond 50 percent, US\$300,000 for each additional 10 percent of procuring entities using the system, up to 100 percent.	
		9.00	2.00	3.00		4.00	
Total		22.937	4.437	3.00	6.50	4.00	5.00



DLI Verification Protocol

#	DLI	Definition/ DLR Description	Scalability of Disbursements (Yes/No)	Protocol to Evaluate Achievement of the DLI and Data/Result Verification		
				Data Source / Agency	Verification Agent	Procedure
Component 1: Strengthening allocative efficiency of public investments, programs and excise management						
DLI 1:	Strengthened public investment management, efficiency and transparency	Definition: This indicator is designed to evaluate the progress of policy and operational measures which will improve the vetting and transparency of public investments. Description: The DLIs are identified based on critical policy and operational measures required to achieve the PDO of improved prioritization of ready public investments with high social economic impact achieved through improved efficiency, transparency and strengthened Public investment management processes. The initial DLI will recognize the government commitment to strengthen the governance mechanism to evaluate and select large public investment projects. It will then incentivize the stringent appraisal and vetting of large investments, a transparent information system for project submission and approval of large project, including through independent reviews expected to lead to greater selectivity of high impact ready projects. Disbursement Linked Results:				
		DLR 1.1 The Cabinet has: (i) approved the establishment of the public investment management committee; and (ii) approved and publicly disclosed the guidelines including climate disaster risk screening.	No	MNPEA	Not Required	Evidence will be cabinet minutes approving the PIM committee and the PIM guidelines. The latter are accessible on the website of NPD, within the Ministry of National Planning and Economic Affairs (MNPEA).
		DLR 1.2 Public Investment Management system is operational and includes	No	MNPEA / IVA	Required	It is a web-based project portal for the submission and clearance of project proposals to NPD and other relevant



		geotagging of projects for citizen feedback.				departments. It includes all key steps in line with the NPD PIM guidelines. It also includes a project monitoring functionality and database and feature for geo-referencing of physical projects and a module for online citizen consultation and feedback. The system is considered operational once it is declared as 'Go live' by the key departments (NPD and Department of Project Management & Monitoring) after successful conclusion of acceptance tests and used by all line ministries for their project submission to NPD as per extant delegation.
		DLR 1.3 80 percent of Large Investments submitted to NPD for review and /or approval have an independent pre-feasibility review published along with the project proposal on the NPD's official website.	Yes	MNPEA /IVA	Required	Evidence will be through the Independent Verification Agent (IVA) assessing the data provided by the Department in charge of planning. Large projects as per circular MNPEA 02-2019 and as updated from time to time. Review of the project proposal by NPD is considered as independent of the line ministry submitting the project proposal.
DLI 2	Increased efficiency of excises	Definition: This indicator measures the progress of development and implementation of an IT based excise management system. Description: the initial DLI is designed to incentivize the finalization of the scope and functionality of the IT based excise management system to implement a modern and transparent Excise licensing and control system.				



Disbursement Linked Results:					
DLR 2.1 Finalization by the excise department of the Functional Requirements defining the scope of the excise management system	No	MoF	Not required	Excise department approves the Functional Requirements of the Excise Management System through an executive order.	
DLR 2.2 New excise management system is operational	No	Dept. of Excise/ IVA	Required	Evidence will be the data provided by the Excise department and verified by the IVA of a representative sample of licenses and permits issued through the system. The system is considered operational once it is declared as 'Go live' by the department through notification after successful conclusion of acceptance tests.	
DLR 2.3 New risk-based excise control system has been rolled out to the largest liquor producer and the largest beer operator in the Borrower's territory	Yes	Dept. of Excise/ IVA	Required	Evidence will be the data provided by the Excise department and the respective operators and verified by the IVA. It is expected to be rolled out to the largest liquor and beer producer each in country (by market share). The specification for the risk -based excise control system will be made available by the Excise Department through a administrative notification.	



Component 2: Improving the operational efficiency of and transparency in Public Expenditures through procurement					
DLI 3	E-procurement system operationalized	<p>Definition: This DLI is designed to measure the development and effective implementation of the government e-procurement system. Which is measured against a set of pre-agreed operational milestones with the counterpart.</p> <p>Description: This indicator will be fully met when all procuring entities use the e-government procurement (eGP) system for their annual procurement plans, the publication of their tenders and for the procurement of their goods and supplies. Civil works contract may still need off-line evaluations considering their heterogeneity and complexity. In order to achieve this target incremental operational steps will need to be completed from finalizing functional and technical specifications, developing and testing the system and rolling it out across ministries. The 'Core Design' functionalities of the system include: a central vender registration module, a module for procurement plans, a standardized classification of goods and services to be procured in line with the UN, the central portal for the publication of tenders and contract awards, a link to MoF budget and accounting system to ensure budget availability, a module for shopping. The e-procurement system will follow the open contracting standards to facilitate disclosure and analysis of procurement data. The e-procurement system will capture gender disaggregated data to monitor and foster female entrepreneurs' access to public tenders.</p> <p>Disbursement Linked Results:</p>			
		<p>DLR 3.1 MoF has finalized the 'core design' of the e-procurement system and officially launched it.</p>	No	MoF	Not required
		<p>DLR 3.2 Procurement plans, and cabinet level tenders and contract awards are published on MoF website</p>	No	MoF/IVA	Required



						by Cabinet at the same time.
		DLR 3.3 The e-procurement system is fully operational and all procuring entities at the central government level are using it.	Yes	MoF/ IVA	Required	Fully operational means availability of all modules as per the 'core design' finalized by the MoF. Evidence of use will be the data on procuring entities using the e-procurement system and generated by the system, compared with the list of central government procuring entities.



VI. RESULTS FRAMEWORK AND MONITORING

Results Framework

COUNTRY: Sri Lanka

Sri Lanka Public Sector Efficiency Strengthening Project

Project Development Objectives(s)

To improve transparency and the efficiency of core government and public financial management functions.

Project Development Objective Indicators

Indicator Name	DLI	Baseline	End Target
Strengthening allocative efficiency of public investments, programs and excise management			
Share of large projects that are vetted by the new Public Investment Management Committee (Percentage)		0.00	80.00
Enhanced operational efficiency of processes in Excise Management (Text)		Manual processes deployed for application, processing and issue of licenses and permits	100% of the licenses, permits and passes are applied for and issued online using the excise management system
Improving Operational Efficiency of and Transparency in Public Expenditures through Procurement			
Reduction in time taken for procurement of standard goods and services (Days)		265.00	159.00
Increase in availability of information to the public on contracts approved and awarded at the Cabinet level (Percentage)		0.00	100.00
Strengthening Governance, Transparency and Efficiency of Public Services			
Improvements in performance ratings of NAOSL in selected priority indicators as per SAI-PMF assessment. (Text)		Scores in Domain B and E between 0 and 1	Scores in Domain B and E increased to between 2-3



Intermediate Results Indicators by Components

Indicator Name	DLI	Baseline	Intermediate Targets				End Target
			1	2	3	4	
Strengthening the allocative efficiency of public investments, programs and excise management							
Increased vetting and transparency of public investments (Text)		In 2017 there was no integrated institutional arrangement to review and vet public investments; guidelines were outdated and did not include climate risks.	DLR 1.1 The Cabinet has: (i) approved the establishment of the public investment management committee; and (ii) approved and publicly disclosed the guidelines including climate disaster risk screening.	Scope, Functionality, design and approach to development of PIM system finalized	DLR 1.2 The Public Investment Management system is operational and includes geo-tagging of projects for citizen feedback.	50 % of the large investments submitted to NPD for review and/or approval have an independent pre-feasibility review published alongwith the project proposal on NPD's website and PIM Project Monitoring Module is updated for at least 30% of projects.	DLR 1.3 80% of Large Investments submitted to NPD for review and/or approval have an independent pre-feasibility review published along with the project proposal on NPD's official website.
Improved efficiency and predictability of excise management (Text)		Absence of a Information Mgt system and outdated excise policy and regulations	Excise Department regulations updated.	DLR 2.1 Finalization by the excise department of the functional requirements defining the scope of the excise management system	DLR 2.2 New excise management system is operational.		DLR 2.3 New risk-based excise control system has been rolled out to the largest liquor producer and the largest beer producer in the Borrower’s territory.
Improving the operational efficiency of public expenditures through procurement							
Improve efficiency of procurement function (Text)		In 2018 there was no electronic procurement system in the Borrower’s territory.	DLR 3.1 MoF has finalized the core design of the e-procurement system and officially launched it.	DLR 3.2 Procurement plans, and cabinet level tenders and contract awards are published on MoF website.	-	DLR 3.3 The e-procurement system is fully operational and all procuring entities are using it	E-procurement system core design functionalities are being used by over 70% of the procuring entities
Number of Accredited		0.00	300.00	500.00	700.00		1,000.00



Indicator Name	DLI	Baseline	Intermediate Targets				End Target
			1	2	3	4	
Procurement staff (Number)							
Percentage of accredited Procurement staff who are women (Percentage)		0.00	20.00	25.00	30.00		35.00
Strengthening the governance, transparency and efficiency of public services							
Proactive disclosure of information by ministries (Text)		2017: 15% of ministries scored MS on their online statutory proactive disclosure.	20 % of the Ministries trained on proactive disclosure requirements	60 % of the ministries trained on proactive disclosure requirements	100 % of Ministries trained on proactive disclosure requirements		50% of all ministries score moderately satisfactory or above for their statutory online proactive disclosure.
Capacity of NAOSL to deliver against their mandate enhanced (Text)		NAOSL performing between the founding and established levels as per SAI-PMF assessment in 2018 at an aggregate level with low scores in Domain B -Internal Governance and Domain E- Human Resources and Training	Detailed implementation plan incl.HR capacity development prepared on the basis of Institutional Development Plan	Strategic Planning, Overall Audit Planning and Quality Assurance units established and/or strengthened and staff trained	At least 250 staff have received specific training Financial Attest Audit, Environment audit , procurement audit and in enhancing report writing skills	Pilot test of a framework of participatory audit involving citizens completed and results shared	Improvement in SAI-PMF Assessment over priority indicator in baseline assessment in Domains B, C (Audit Quality and Reporting) and E
Capacity of officials in the civil division of the Attorney General Office enhanced (Text)		Low level of investment in enhancing the capacity of officials in the office of Attorney General	Training Need analysis completed, training plan developed and approved by the Attorney General's Office and 30% officials have recd. initial training	40 % of the Officers have received training consistent with the identified training needs	50 % of the Officers have received training consistent with the identified training needs	70 % of the Officers have received training consistent with the identified training needs	80 % of the Officers have received training consistent with the identified training needs



Monitoring & Evaluation Plan: PDO Indicators

Indicator Name	Definition/Description	Frequency	Datasource	Methodology for Data Collection	Responsibility for Data Collection
Share of large projects that are vetted by the new Public Investment Management Committee	% of large projects vetted, prioritized and approved by the Public Investment Committee	Annual	NPD Annual Report on Large projects	Large projects as per circular MNPEA 02-2019	Department of National Planning
Enhanced operational efficiency of processes in Excise Management	% increase in permits, licences and passes issued online	Annual	Department of Excise	Progress Reports from Excise Dept	Department of Excise/ Ministry of Finance
Reduction in time taken for procurement of standard goods and services	% in reduction of average time from advertising to award	Annual	Ministry of Finance/ Department of Public Finance	Information generated from the e-procurement system	Ministry of Finance
Improvements in performance ratings of NAOSL in selected priority indicators as per SAI-PMF assessment.		In the final year of the Project	SAI-PMF reassessment of NAOSL	Independent SAI-PMF Assessment	NAOSL
Increase in availability of information to the public on contracts approved and awarded at the Cabinet level					



Monitoring & Evaluation Plan: Intermediate Results Indicators

Indicator Name	Definition/Description	Frequency	Datasource	Methodology for Data Collection	Responsibility for Data Collection
Increased vetting and transparency of public investments	As per DLI/ DLR Verification Protocol	Six monthly Project Progress reports and as per DLI/ DLR Verification Protocol	Ministry of Finance and Project Management Unit progress reports and IVA reports	Report from MoF PMU, verified by IVA.	NPD, Dept of Project Monitoring and Management,
Improved efficiency and predictability of excise management	As per DLI/ DLR Verification Protocol	As per DLI/ DLR Verification Protocol	Ministry of Finance and Project Management Unit	Report from MoF PMU, verified by IVA	Excise Department
Improve efficiency of procurement function	Measures the progress in the development, implementation and roll out and use of the e-procurement system	Annual	As per Project progress Reports and DLI/DLR verification Reports	Report from MoF PMU, verified by IVA	PMU and PFD
Number of Accredited Procurement staff	No. of total accredited staff	Annual	National Procurement Commission	NPC records	National Procurement Commission



Percentage of accredited Procurement staff who are women	Percentage of total accredited staff who are women	Annual	National Procurement Commission	NPC records	National Procurement Commission
Proactive disclosure of information by ministries	Measures the improvement in capacity to and the quality of proactive disclosures by ministries as per the RTI and	Annual	Ministry of Finance and Project Management Unit	End line survey consistent with the methodology adopted as per the Verite Research Assessment methodology published by DoI	Department of Information and RTI Commission
Capacity of NAOSL to deliver against their mandate enhanced	Improvement prioritized indicators as per SAI-PMF re-assessment over baseline	Annual	NAOSL	NAOSL Progress Reports and SAI- PMF Reassessment	NAOSL
Capacity of officials in the civil division of the Attorney General Office enhanced	% of officers from the civil division having received the capacity building	Annually	Attorney General's Department	Report from Attorney General's Department	Attorney General's Department



ANNEX 1: Implementation Arrangements and Support Plan

COUNTRY: Sri Lanka

Sri Lanka Public Sector Efficiency Strengthening Project

Project Institutional and Implementation Arrangements

1. The institutional responsibilities and arrangements for project implementation will be established for the participating ministries and agencies at the national level. The project is fully integrated within the GOSL administration, and the project implementation is designed to capitalize on existing government agencies at all levels. The project will be implemented using a multi-stakeholder approach – the various stakeholders involved in the project are expected to contribute to project implementation in a coordinated manner. The participating departments/agencies will carry out project activities within their mandates, but with overall coordination and managed by the PMU.
2. **High-level Project Steering Committee (PSC).** A PSC will be established within six months of effectiveness, in the Ministry of Finance (MoF), chaired by the Secretary to the Treasury or his representative and comprising the Secretaries or Additional Secretaries of the Ministries involved (as designated), the Project Director and the heads of the independent institutions involved in the project, namely: Attorney General's Department, Auditor-General's Department, Excise Department, Right to Information Commission, and National Procurement Commission. The WB and the EU may be represented as observers as per the GoSL- EU financing agreement. The PSC will convene at least twice a year to review overall project progress and implementation performance. The PSC will provide strategic guidance on project activities and oversight for the project implementation; ensure effective coordination and communication among the project stakeholders; review the progress of the project and provide directions/remedial solutions as appropriate. In case the PSC does not convene at least once a year or as required for the sound project implementation, the Operational Committee will carry out the functions and responsibilities of the PSC.
3. **Operational Committee (OC).** The Operational Committee (OC) will be set up in the MoF and chaired by the Project Director. The Project Management Unit will serve as the permanent secretariat of the OC. The OC will include the relevant Directors -General of the participating departments. The OC will convene at least every quarter to provide technical guidance and inter-agency coordination for project implementation. The OC will review project activities, operational and financial progress and report to the PSC on project implementation and proposed decisions to improve implementation and impact; ensure effective monitoring and reporting, enhance coordination, advise on any measures to strengthen project implementation; guide the overall learning and knowledge dissemination activities; and consolidate implementation lessons for sector policy formulation.
4. **Project Management Unit (PMU).** The PMU will be set up under the Ministry of Finance, within six months of Effectiveness. The PMU will be led by a Project Director and comprise a team including: a project coordinator supporting the Project Director, a Financial Management Specialist/Accountant; a Procurement Officer; and a M&E officer. The PMU will: ensure all project activities are planned, financed and implemented as per the project annual work program and budget, oversee the implementation of the project activities; manage and coordinate project implementation; act as secretariat for the PSC; carry out procurement under the project in collaboration with technical specialists/focal points in the departments responsible for the individual thematic reforms initiatives and also provide procurement



support to the project team; undertake financial management (FM) functions; monitoring and report on project performance, DLIs and corresponding evidence; and manage the project-level grievance and complaints procedures pursuant to the Project Operations Manual (POM) for the specific activities under the respective pillars. The project annual work program will be prepared jointly with the component focal points and specify the priority activities to be carried out for their respective components, the estimated timeline, costs and who will be responsible for that. This will complement the project procurement plan. The work plan will also specify who needs to do what and when to meet the agreed DLRs. As the technical work has continued throughout project preparation, most of the first year DLRs have been met or are about to be met, including the establishment of the Public Investment Management Committee and Guidelines and the launch of the e-procurement system. On the technical assistance side, the following priority activities have been identified: (i) the development of functional and technical specifications for the public investment management system, (ii) the development of the National Evaluation Framework, operationalizing the policy, (iii) the excise business process review, (iv) the guidance note to ministries on the proactive disclosure of information, (v) the development of the policy on participatory audits by the NAOSL, and (vi) the training needs assessment for the AGD. Terms of reference have been prepared for these activities, increasing project readiness.

5. **The Project Operations Manual shall be adopted no later than six months after the signing of the legal agreement.** The POM shall set forth, inter alia, the following detailed arrangements and procedures for the implementation of the Project: (a) institutional arrangements for the day to day execution of the Project; (b) budgeting, disbursement and financial management arrangements; (c) Project monitoring, reporting, evaluation and communication arrangements; and (d) any other administrative, financial, technical and organizational arrangements and procedures as shall be necessary for the implementation of the Project and the achievement of its development objective.

6. **The National Audit Office of Sri Lanka will have a dedicated project team that will implement the activities of its sub-component under the guidance of the PMU.** This project team will be responsible for (i) managing and implementing the NAOSL's sub-components and activities; (ii) payment for project related activities; and (iii) periodic reporting on physical / financial progress against the project to the PMU. FM and procurement activities will be carried out by the project team, by delegation from the Project Director/ PMU. The fiduciary capacity of the NAOSL's Department has been assessed as adequate, including based on past positive experience in implementing prior World Bank projects. Agencies and commission supported by the project other than the NAOSL will designate focal points for the implementation of their respective activities, coordination, monitoring and reporting in cooperation with the PMU. These focal points will not carry out procurement and fiduciary management directly, as this is being centralized at the PMU.

Financial Management, Disbursements and Procurement

7. **Overall responsibility for Financial Management (FM) will rest with PMU established under Ministry of Finance (MoF), which is the primary implementing agency.** FM responsibilities include: ensuring compliance with all financial covenants in the project legal agreements; and the Disbursement letter (DL). The PMU will be responsible for budgeting of the project activities, obtaining funds from the loan/ grant, management of relevant fund transfers to the NAOSL, making project related payments, accounting and collation/ preparation of project financial reports and; submission of claims to the World Bank; managing and coordinating external audits; furnishing financial reports and project audit reports to WB.



8. **Budgeting.** The PMU will forecast the required resources to be budgeted in consultation with the various departments and agencies, which will form the basis for it to be incorporated into the annual budget. A separate budget code/s (line item/s) will be set up for project activities under MoF under foreign financing of the TA component. The PMU and the NAOSL's project team will prepare detailed implementation plans in line with the detailed project budget to clearly specify the funding requirement under each component and activity that they implement. Project funds will flow to, and will be handled by, the PMU at MoF and Project Team at the National Audit Office of Sri Lanka only.

9. **FM staffing.** The Financial Management Unit of the PMU will be headed by a qualified and experienced accountant, preferably with prior experience in managing FM arrangements under World Bank or donor-financed projects with appropriate FM support staff assigned or recruited for the project. The FM unit in the PMU will be responsible for managing day-to-day FM activities, including: project budgeting, disbursement planning and forecasting; operation of the designated account (DA), including claiming replenishments, project related payments and disbursements, accounting and reporting ; fund transfer consolidation and submission of quarterly consolidated IUFRs and annual project financial statements; and ensuring timely audit and submission of project financial statements to the Bank. The FM staff in the Auditor General's PT will also be responsible for similar FM functions and liaising with the PMU. Training will be provided to the PMU and PT FM staff on the project and disbursement arrangements in the initial stages of the project.

Fund flow and disbursement arrangements

10. **Designated Accounts.** The applicable disbursement methods are: advance; direct payment; and re-imbursement. Both World Bank and the EU funds allocated to recipient-executed activities will be transmitted to two Designated Accounts (DA) opened for MoF. Advances, if required, from the World Bank and EU will be deposited in the respective DA's. The ceiling to the advance to DA will be variable and the advances will be made on the basis of the six-month projected expenditures. The DAs will be US\$ denominated segregated accounts and will be opened at Central Bank of Sri Lanka (CBSL) with a unique subledger number and will be managed by the PMU. Disbursements will be report-based. PMU will submit quarterly Interim Unaudited Financial Reports (IUFRs) to the WB within 45 days of end of each quarter which will also be the basis of Withdrawal Applications (WAs) for replenishments to the DAs, reporting of use of DAs funds and documentation of expenditures. Category 2 expenditures maybe reimbursed.

11. The IUFR prepared for Category 1 activities, will capture items defined in the Eligible Expenditure Program (EEP) and this may be submitted to World Bank on a semi-annual basis within 45 days of end of reporting period for reimbursement and for Category 2 activities will report expenditure under the TA activities.

12. **Local Currency Accounts.** For the TA Component, the PMU and PT in the Auditor-General's office will also open and operate a dedicated Sri Lanka rupee (LKR) account which will be used to make payments for eligible expenditures and track the inflow and outflow of project funds. Exchange losses arising due to the transfer from the DAs to LKR account will not be considered eligible expenditure for financing by the World Bank or EU. The PMU will also have the option of requesting a direct payment to suppliers through CBSL using the proceeds in the DAs.

13. **Accounting policies and procedures.** The project's accounting practices will be governed by the generally accepted accounting principles, financial regulations and applicable circulars. Bank accounts will be reconciled on a monthly basis; financial reports/statements will be prepared on monthly basis to facilitate monitoring of the progress of the Project. The expenditure reports from Government's financial



reporting system, supplemented by Excel-based spreadsheets for capturing component-wise expenditure will be used for generation of financial information of the project. This will facilitate preparation of expenditure reports by budget classification and project component and subcomponents enabling comparison with the budget/components and effective monitoring of expenditure. All documentation for the expenditures reported for disbursements will be retained at the PMU, PT and line departments which will be made available to the external auditors and to the WB and EU as required.

14. **External audit:** The external audit of the project will be carried out by the Auditor-General's Department other than the sub-component implemented by the Auditor-General's Department. Financial statements of the sub-component being implemented by the NAOSL will be audited by the independent private auditor that audits the Auditor-General's Department as part of their entity audit. Such entity audit report of the Auditor-General's Department will reflect separately a disclosure on the project financed activities. Audit reports will be submitted to the World Bank within six months after the end of the financial year. The following audit reports, mentioned in Table 3 below, will be monitored for submission to the World Bank.

Table 3. Audit Reports

Implementing Entity	Audit Report	Auditor	Date
PMU (Ministry of Finance)	Project Financial Statements (covering TA)	National Audit Office of Sri Lanka	June 30 each year
PMU (Ministry of Finance)	National Financial Statements (covering EEP)	National Audit Office of Sri Lanka	June 30 each year
PT (NAOSL)	Entity Financial Statements with disclosure on project sub-component	Private Auditor	June 30 each year

15. **Implementation support plan.** The FM risk rating is moderate. Consistent with a risk-based approach to FM supervision, FM supervision activities will consist of desk reviews of external audit reports, including verification of the adequacy of the resolution of major audit observations, and reviewing quarterly IUFs, supplemented by dialogue with PMU/PTs as needed, especially during the initial years of project implementation. The FM supervision mission will be conducted at least once every six months. Other supervision tools and resources, such as transaction reviews and site visits, will be used in an effort to periodically monitor the adequacy of the FM system. Significant training/ hand-holding to the project FM staff will be required in the initial stages of the project to help ground the results-based disbursement arrangements.

Disbursement Arrangements:

16. **Disbursement will be against the eligible expenditures.** Retroactive financing is possible up to 20 percent of the project's budget and of expenditures incurred 12 months prior to the signing of the Loan Agreement. Existing fiduciary management arrangements/systems in MoF assessed to be satisfactory to WB, will be used to incur retroactive expenditure.

17. The disbursements against DLRs will be made to the GoSL consolidated fund in LKR on the basis of satisfactory achievement of DLRs and verified according to the agreed verification protocol, including by an IVA, as appropriate, supported by reported EEP.



18. For that purpose the GoSL shall (i) appoint and thereafter maintain, at all times during the implementation of the Project, the IVA under terms of reference acceptable to the Bank, to verify the data and other evidence supporting the achievement of the DLRs; (ii) ensure that the Verification Agents carry out verification and process(es) in accordance with the Verification Protocol; and (iii) submit to the Bank the corresponding verification reports in a timely manner and in form and substance satisfactory to the Bank. In the event there is a need for verification services prior to the appointment of the IVA, put in place adequate interim arrangement satisfactory to the Bank and approved in writing by the Bank for verification of the DLRs.

19. On validation of DLRs achieved, the project will seek reimbursement from the World Bank of an amount equivalent to the DLR value achieved. The World Bank, subject to the EEPs being adequate to cover the value of DLRs achieved, will disburse the full amount. Where the reported EEP is less than the aggregate DLR value achieved by the project, disbursement by the World Bank will be limited to the value of the reported EEP. The balance DLR value will be reimbursed when an adequate EEP is reported subsequently. The reported EEP will be considered cumulatively;

20. If the project does not achieve the DLR targets for a particular year, the Bank may agree for rollover until the DLR is achieved; or reallocate all or portion of the loan proceeds to other DLRs and/or cancel in whole or part any withheld amount of the proceeds of the loan allocated to the said DLR(s). The expected schedule of reporting of DLIs and DLRs, its verification, and disbursement are given in Table 4.

Table 4. Expected schedule for DLI/ DLR reporting, verification, and disbursement

Year ending June 30	DLI report due date	Verification due date	Disbursement	Expected disbursement (US\$ millions)
2020 (Year 1)	May 2020	June 2020	June 2020	3.50
2021 (Year 2)	April 2021	May2021	June 2021	1.00
2022 (Year 3)	April 2022	May 2022	June2022	0.00
2023 (Year 4)	April 2023	May 2023	June2023	6.00
2024 (Year 5)	April 2024	May 2024	June2024	7.50
2025 (Year 6)	October 2024	November 2024	December 2024	5.00
Total				23.00

21. **The Eligible Expenditure Program. The Eligible Expenditure Program.** Given the cross cutting nature of reforms especially e-procurement and Public Investment Management, which will extend to and impact the whole of the Government, eventually covering all the ministries, Departments , spending agencies and State owned enterprises, the successful implementation, adoption and successful roll out of the two initiatives will require the identification, participation and active involvement of officials at all levels across the government. These two reforms are likely to involve approx. 3000 officials, with several identified reform champions, extensively involved in e-procurement and project planning and monitoring. Similarly, the excise management system is intended to automate all the processes in the excise department (client facing and back-end internal processes, as a work flow-based system), which will require the active engagement of almost all the excise officials, which currently relies on manual paper-based processes. The EEP therefore includes (i) non-procurable investments required for the sensitization, change management, capacity building and roll of out the three IT applications; (ii) costs of peripheral hardware, servers and operational costs etc. (especially for the excise department) and (iii) a share of the



salary costs of departments officials who will be directly involved in the design, development and roll out of the solutions¹³. These are considered essential and appropriate implementation of activities to achieve the PDO's, as ownership and active involvement of key stakeholders is a critical element for the successful adoption of the IT driven reforms. These are distinct from the activities proposed to be financed under the technical assistance component. A summary table of the EEP is given in Table 5.

Table 5. Eligible Expenditure Program

US\$ Mn	2019	2020	2021	2022	2023	2024	Total
IT related hardware, training, capacity building and hand-holding implementation support for the 3 IT applications							
E-Procurement Systems	0.10	0.30	1.10	0.60	0.40	0.30	2.80
Excise Management Systems		0.10	1.30	1.60	0.70	0.50	4.20
PIM systems		0.10	0.20	0.60	0.70	0.40	2.00
Sub-Total	0.10	0.50	2.60	2.80	1.80	1.20	9.00
Share of salaries of core departments							
National Budget Department *	0.60	0.60	0.61	0.61	0.62	0.63	3.67
Public Finance Dept **	0.29	0.29	0.29	0.30	0.30	0.30	1.77
Excise Dept ***		2.87	2.92	2.96	3.00	3.05	14.80
Department of Project Mgt. & Monitoring *	0.29	0.29	0.29	0.30	0.30	0.30	1.77
National Planning Dept *	0.40	0.40	0.40	0.41	0.41	0.42	2.44
Share of salaries of core departments	1.58	4.45	4.51	4.58	4.63	4.70	24.45
Annual EEP	1.68	4.95	7.11	7.38	6.43	5.90	33.45
EEP (@ 70 percent reimbursement)	1.18	3.47	4.98	5.17	4.50	4.13	23.42

* primary stakeholders in Public Investment Management System

** primary stakeholder in e-Procurement

*** primary stakeholder in Excise

22. The Government has a well-established process & controls in place for the payment of personnel costs such as direct transfer from treasury to employees' bank accounts, internal controls over changes to personnel records and the payroll records, adequate segregation of duties with regard to payroll preparation etc. Also controls & mechanisms existing in the Government, for payments related to procurement of IT systems & equipment is also found to be satisfactory. This comprises of processes & controls in place for tracking payments as per contractual obligations, entering payment data into systems & payments to suppliers “

¹³ In lieu of extrapolating a small share of salary costs across all line departments who are likely to be directly involved in implementation and roll out only a share of the salary of the primary departments has been considered for the purpose of EEP



23. **Disbursement schedule.** Loan funds will be disbursed against the TA component and the DLIs achieved, under the following categories subject to the allocated amount, reported EEP, and the disbursement percentage as indicated in Table 6.

Table 6. Disbursement schedule

Category	Amount of the Loan Allocated (in US\$) ¹⁴	Percentage of expenditures to be financed (inclusive of Taxes)
(1) Eligible Expenditure Program (EEP) under components/ Parts 1.1(b), 1.2(b) and 2(b) of the Project.	22,937,500	70 percent
(2) Goods, non-consulting services, consulting services, Incremental Operating Costs and Training under components/ Parts 1.1(a), 1.2(a), 2(a), 3.1, 3.2, 3.3 and 4 of the Project	2,000,000	100 percent
(3) Front-end Fee	62,500	Amount payable pursuant to Section 2.03 of this Agreement in accordance with Section 2.07 (b) of the General Conditions
(4) Interest Rate Cap or Interest Rate Collar premium ¹⁵	Nil	Amount due pursuant to Section 4.05 (c) of the General Conditions
TOTAL AMOUNT	25,000,000	

24. **Retroactive financing.** Retroactive financing facility under the project may be needed for eligible expenditures up to a maximum of US\$5 million for payments made from January 1, 2019 against project related expenditures procured in accordance with applicable World Bank procurement guidelines.

Procurement

25. **Implementation of the project will be supported by a procurement plan will be procured by the PMU/PT in accordance with the Bank's Procurement Regulations for IPF Borrowers (July 2016) revised November 2017 and August 2018 ("Regulations").** In addition, some procurement activities are expected to be carried out by the National Audit Office of Sri Lanka. Procurement will consist mainly of small value items and some servers and related IT hardware for the IT systems financed under the project, and to support rollout and dissemination of these systems. An assessment of procurement capacities and implementation risks for both procuring entities has been conducted. Although the procurement activities for the project are centralized at the PMU at MoF and the PT at the AGDSL, it is not expected to be a substantial workload, and the procuring entities will be staffed adequately. The main procurement risks identified by the assessment are: inadequate procurement capacities; limited previous experience in implementing a Bank-financed project; inadequate experience in contract administration; and

¹⁴ If the Loan is made in more than one Currency Tranche, an additional column for each additional Currency Tranche would be required, so as to set out the amount in each Currency allocated to the particular Categories.

¹⁵ Include bracketed withdrawal category ONLY if the Borrower has elected caps and collars **AND** requested to finance the premia out of the proceeds of the loan. The amount allocated to this category will be zero until premia is to be charged.



coordinating procurement across various components of the project. The agreed upon risk management measures include: PMU will engage full-time procurement specialists having experience in World Bank procurement procedures for the entire project implementation period and train existing procurement staff, specifically on fraud and corruption flags, and on addressing complaints; preparation of an annual procurement progress report by the PMU to share with the Bank, to include, inter alia, procurement plan updates, action on findings of post reviews and other procurement and contract administration issues; implementation of a monitoring mechanism for procurement by the PMU, which will include implementation, as well as the defects liability phase and warranty phase of contracts. The newly created independent commissions do not yet have staff nor project implementation experience. The Bank will continue to provide direct support to these commissions, including through the World Bank-administered EU Trust Fund, while ensuring their institutional strengthening.

26. **The project has prepared a PPSD that addresses market risks for the procurement to be carried out.** Given the nature and limited size of the procurements, no major market risks are envisaged. A procurement plan for the project has been prepared and agreed.

27. **It is expected that some of the activities may be implemented through twinning arrangements¹⁶.** Any contracts to be procured under such arrangements will be included in the procurement plan, and subject to the Bank's regulations. The recipient-executed portion of the EU Trust Fund will also be procured under the regulations. Capacity building and training will be conducted under an agreed training plan, which may include training provided by government training institutions.

Training and capacity building approach

28. **The important reforms led by the Government to foster a more open and inclusive mode of governance imply a new way of public sector *modus operandi*.** The 19th constitutional amendment introduced greater access to information, strengthened overall public-sector governance and accountability of its institutions. Although important progress has been made on the policy and legal front, implementation of these reforms is still work in progress. The changes demand from the public sector a new way of functioning: transitioning from individual teams and departments carrying out limited process-oriented activities to a more collaborative, outcome oriented and performance-based style of working. Since the Ministry of Finance leads the implementation of the reforms, it is precisely there, where most organizational changes need to happen.

29. **The reforms have important implications for the functions, organization, processes and skills mix of these departments.** They will need to adapt and respond to the broader reform agenda and changing nature of work through (i) greater integration and synergies across departments and reforms, (ii) a more open, collaborative and inclusive work culture, (iii) increased decentralization and devolution of functions, (iv) a stronger focus on public policy objectives and performance beyond compliance; (v) the generation, use of information.

30. **Functional skill-mix needs assessment.** The project will support the preparation of a functional training needs assessment matching the organization's evolving strategic functions, processes and

¹⁶ Learnings for past experiences of Bank and non-Bank funded IT reforms in Sri Lanka, the traditional approach, which assumes that the full scope is designed and agreed prior to procurement and on-boarding of an IT vendor has shown less than satisfactory results. Instead, an agile approach based on twinning/ partnership with countries which have successfully implemented such reforms is proposed to be explored and where feasible adopted. Such an approach in e-procurement, wherein experts responsible for implementing e-procurement in Georgia have been twinned with local IT experts in the University of Colombo is showing encouraging results. Similar approach is proposed for excise solution with potential learnings from successful IT led reforms in excise from Thailand and India



workloads with the required skills mix and current skills gaps. The analysis will identify the overall needs of key public servants, but also specific needs for groups of professionals, such as Senior Officials and midcareer public servants involved in these new functions.

31. **Rolling out a department capacity building plan.** The project will support the preparation of a capacity building plan addressing this skills gap through various means, including different types of training. The project will identify a nodal unit in the respective department in charge of the design and implementation of the capacity building plan. The capacity building plan will cover both thematic and cross cutting areas. Thematically the training will focus along the core functional areas of the department. For the Treasury, this will include public financial management, procurement, debt and treasury management, macro fiscal management, internal auditing, public investment management and M&E or public projects, programs and policies, among others. Additionally, the training plan will include other cross cutting aspects that are deemed necessary based on the functional review and skill mix needs assessment. These might include communications, people and human resource management and leadership and personal development courses.

32. **Training modalities and training partnerships.** The modalities of the training will also include a wide range of options including on the job training, face to face short and long-term courses and seminar, online courses and training abroad. The project will develop partnership with local and international organizations and academic institutions to identify available courses or develop specific training courses based on local needs. The project will explore alternative modalities such as twinning arrangements with other international organizations in collaboration with Development Partners, temporary collaborations with private sector institutions and lateral entries of mid-career professionals to the public sector as part of the civil service career

33. More specifically, the project's technical assistance and capacity building component will support the following indicative activities mentioned in Table 7 below.

Table 7: Indicative list of proposed TA Activities

Strengthening capacity and skills of key central departments and institutions	
Valuation Department	<ul style="list-style-type: none"> • Functional Training Needs Assessment and plan • Training and capacity building based on training plan, including soft skills and on the job training
Public Investment Management	<ul style="list-style-type: none"> • Technical Assistance to NPD and to the Public Investment Committee and Dept. of Project Monitoring and Management • Short term expertise and TA to develop the PIM information system and overseeing its development and implementation • National Evaluation policy -pilot implementation
Excise Reforms	<ul style="list-style-type: none"> • Excise Business process review and Project Management Consultancy support • Short term expertise and TA to design the scope of the Excise system • Advisory and analytical work



Procurement Reforms	<ul style="list-style-type: none"> • TA to the National Procurement Commission • Roll out strategy and material for the new E-GP system • Short term expertise and TA to develop the e-GP • Advisory and analytical work, including on green procurement • Open Contracting database
Implementation of Right to Information	<ul style="list-style-type: none"> • TA to the Right to Information Commission • Training Information Officers • Implementation support to 5 pilot ministries on proactive disclosure of information • Survey update on the online proactive disclosure of ministries using the WB- Verite methodology used for the baseline. • Outreach and communication, including demand side
Implementation of the Audit Act	<ul style="list-style-type: none"> • Technical Advisors to the NAOSL Task Force and Senior Management • Organization Review of the NAOSL • Survey of the SOE Sector and the development of the NAOSL strategy for the audit of SOEs; • Preparation of NAOSL Strategic Plan • Addressing weaknesses in NAOSL Planning – Development & Implementation of NAOSL Risk Based Annual Operational Plan • Training and Capacity Building over 5 years
Attorney General's Department (Civil Division)	<ul style="list-style-type: none"> • Functional Training Needs Assessment and plan • Knowledge production (handbooks), repository (e-library) and support the department's legal researchers and counsels and other staff, • Training and capacity building based on training plan, including soft skills and on the job training
Treasury Department	<ul style="list-style-type: none"> • General PFM/ PFM Act awareness raising and training • Advisory and TA on debt, fiscal and budget management, ITMIS, transition to accrual accounting, treasury operations. • Training and capacity building based on training plan, including soft skills and on the job training

Economic and Financial analysis of the project

34. **The project is expected to have a positive financial and economic impact through the improvement of the allocative and operational efficiency of Sri Lanka's public finances, thus having an important multiplier effect.** The cost of inputs to the project is mainly investment in IT applications to improve PFM efficiency, staff inputs critical for the successful adoption of the various IT solutions and technical assistance, valued at US\$32.5 million.¹⁷ The benefits will be mainly the efficiency gains expected from the following reforms and project activities. While some of the benefits may be small in percentage

¹⁷ Table 5 defines the Eligible Expenditure Program as salaries of the departments associated with the project. The cost of inputs is expected to be US\$23 million through DLIs, and US\$9.5 million through technical assistance.



terms, they apply to economy-wide or central government-wide expenditure items and may thus result in very large returns compared to the cost of the project (Table 5). This is a conservative estimate of the rate of return of the project, as input costs are fully accounted, but some of the benefits have not been included.

35. **Savings on procurement (component 2).** It is expected that strengthening procurement will lead to economies of scale and more efficient prices. The benefits would apply to the procurable part of fiscal expenditure, which is proxied by purchases of goods and services (LKR 161 billion) and domestically-financed public investment (LKR 390 million).¹⁸ It is assumed conservatively that reforms can reduce the procurement expenditure by 1 percent annually relative to the baseline. (see Table 8 below)

Table 8. Projected cost of inputs and changes in revenue and expenditure compared to baseline

		US\$ million					
	Present value		2020	2021	2022	2023	2024
Discount rate	4.1 percent	6.8 percent					
Value of inputs	23	22	0	5	6	6	5
Value of benefits	65	61	0	10	21	31	42
Savings on procurement			0.0	10	21	31	42
Internal rate of return	22.1 percent	20.4 percent					

Note: only the first 5 years of the project benefits are shown.

Source: MoF, CBSL, World Bank staff projections

36. **The present value of benefits, expressed as reductions in fiscal cost or increases in fiscal revenue, are projected to greatly outweigh the input costs, leading to a substantial internal rate of return, well above the cost of borrowing for this project.** The Present Value (PV) of inputs is between US\$22 and US\$23 million, depending on the discount rate chosen,¹⁹ while the PV of the benefits is estimated between US\$61 million and US\$65 million.

37. **Qualitative benefits and economic benefits.** There are also other expected benefits that are difficult to quantify or that have economy-wide benefits.

38. More stringent selection of public investments using objective economic and social impact and readiness criteria lead to higher return on investment, reduced delays and reduced costs of rehabilitation (sub-component 1.1). It is expected that improvements in efficiency in public investment management will manifest themselves through the overall quality of the projects, lower cost overruns due to delays,

39. Excise reforms are expected contribute to process efficiencies and transparency through ease of doing business, by online rendering of various services and reducing leakage (holograms/ barcodes etc) consequent to implementation of an excise management system. Experience from other economies in

¹⁸ It is assumed that foreign project loans are mostly procured outside Sri Lanka, using different procurement systems, hence they would not benefit from improvements in procurement in Sri Lanka.



South Asia suggest a significant increase in excise revenue on successful implementation of such systems²⁰ through better monitoring of the supply chain and compliance.

Gender assessment and approach

40. **Gender analysis of select public expenditures and procurement aims to reduce the budget's gender blindness and increase awareness of gender impacts, building on the government's 2020 strategy to increase women's economic empowerment and the measures included in the 2018 Budget.**

A recent review of gender budgeting in Sri Lanka²¹ shows that there is a lack of sector specific gender analysis that can inform the budget preparation, resulting in a disconnect between policy objectives and the financial allocations. Gender analysis of public expenditures conducted in neighboring countries have confirmed that the budget allocations directed toward women's policies are extremely low. Under Component 3 the project will: assess the current practices gender sensitive budgeting in Sri Lanka; identify training needs and build capacity of key stakeholders (including gender focal points in MoF, MNPEA and select line ministries) in gender sensitive budgeting.

41. **The project will promote female entrepreneurship by facilitating female entrepreneurs' opportunities to participate in public tenders.** A 2014 report indicates that in Sri Lanka 22.6 percent of women were own account workers as against 36.4 percent for men. The government plans that 40 percent of the jobs created by 2020 should employ women and encourages women's greater involvement and leadership in SMEs. Under component 2, as a pilot program, the project will analyze how women led SMEs benefit currently from public procurement in either the Health, Industries or Agriculture sectors and their constraints to be awarded tenders. Based on the findings the project will select one sector and conduct initiatives under two main areas: (1) ensuring a public procurement environment where measures are introduced to help reduce challenges for female-owned firms in accessing public contracts in the selected sectors, increasing capacity of procurement staff to better target and engage with women-owned SMEs etc and (2) provide women-owned SMEs specific assistance to help them participate better in public procurement markets by improving their awareness and knowledge of public procurement opportunities and requirements, improve women-owned SMEs' capacity to reach public procurement through training workshops which will be conducted in collaboration with Civil Society Organizations (CSOs)/Women's Chamber of Commerce, IFC etc. The impact of this pilot program will be measured by a Gender disaggregated indicator reflecting the increase in women owned SMEs registering as vendors.

42. Acknowledging that there are currently no female accredited staff in procurement, the project will also seek to address this gender gap by encouraging women's formal accreditation for procurement functions. The impact of this work will be monitored under the indicator "Percentage of accredited Procurement staff who are women".

43. **The project will increase women's engagement in the participatory audit processes of the National Audit Office of Sri Lanka developed under the citizen's engagement component through targeted public awareness campaigns.** The project will analyze women's participation in social audits.

²⁰ In the Indian state of West Bengal the excise revenue has shown a compounded annual rate of growth of 10 percent over a 4 year period following implementation of an IT based excise management system as well as significant improvement in industry service standards.

²¹ The 2018 UN Women Report (draft) titled "Gender budgeting initiatives in Sri Lanka: Achievements and way forward"



Climate and disaster impact screening and climate co-benefits

44. **Vulnerability context in Sri Lanka.** The most frequently reported disaster events in Sri Lanka are floods, droughts, landslides and storm surge and cyclones. Extreme Precipitation and Flooding occurs annually in Sri Lanka during the monsoon months resulting huge economic losses. Increasing occurrence of natural disasters is having an adverse impact on growth, budget, external sector and poverty reduction. Average long-term annual losses are estimated at LKR 50 billion which is equivalent to 0.5 percent of GDP or 3 percent of the total government expenditure. Recurring natural disasters, such as flood, landslides and droughts with an estimated long-term, annual average impact of LKR 50 billion (or US\$327 million) knocked budget execution off track. Reducing the direct disaster economic loss in relation to GDP by 2030 is included as an objective in the PIP-2017-2020. It corresponds to the national target (in monitoring and implementation of the Sendai Framework for DRR) of 50 percent reduction of direct economic loss in relation to the GDP (2005-2015) by 2030.

- **Extreme Precipitation and Flooding** occurs annually in Sri Lanka during the monsoon months. May 2016 floods and **landslides**: 93 deaths, 58,925 partially or fully damaged houses, over 100,000 displaced people, and economic damages and losses of about LKR 100 billion May 2017 floods: 213 deaths, 88,000 partially or fully damaged houses, over 100,000 displaced people, and economic damages and losses of about LKR 70 billion. Heavy rainfall across the country in May 2017 resulted in severe landslides and floods in fifteen (15) districts that resulted over 200 deaths mainly due to landslides. Most landslides appear to have occurred only within the Southern, Uva, Sabaragamuwa and Central provinces, and in the peripheries of the Western Province bordering the Southern Province in Sri Lanka. The total recovery needs are estimated at LKR 116 billion. May 2018 floods: 24 deaths, 6,750 partially or fully damaged houses, 172,000 people affected (economic losses were not assessed). More intense rainfall and more flooding is projected in the wet zone of the country and flood mitigation and reducing the impact of flooding in major river basins is a high priority for GoSL.
- **Landslides** had been traditionally considered as an insignificant disaster and now a common occurrence in the hilly areas of Sri Lanka. In May 2017, 35 major landslides occurred causing the majority of deaths from the disaster events, 176 out of 219. The limited fiscal space to include build back better guidelines and Disaster Risk Reduction is a major constraint to adaptation in landslide prone areas.
- **Drought**: the dry zone of the country is exposed to drought more frequently. 2016 to 2017 drought: Approximately 2 million people affected; Government expenditure was LKR 24 billion. Compared with the past 30 years, rainfall during the North–Eastern monsoon season in 2016 was highly erratic and far below average in many parts of the country. More than half of the year’s total precipitation fell in May 2016, while little rain arrived during the October–November inter-monsoon period. A number of reservoirs have already dried up completely. The consequential prolonged dry spell over the entire country meant that one-third of the normal paddy farms were not cultivated during the main “Maha” agricultural season (from Sept–March). Moreover, out of the total area cultivated, over 137,017 hectares were destroyed due to a lack of water for irrigation and there was further yield loss due water stress. Food insecurity is widespread and increasing in drought affected areas. The prolonged droughts are more likely in the future in the dry zone. The Agricultural loss is likely to increase and there may be food insecurity and drinking water shortage.



- **Strong winds** (70-80 km per hour) are more frequent now. More localized high wind caused damages to house in some districts in Sri Lanka. There were high winds associated with the southwest monsoon rains in May and June 2018. The maximum wind speed from tropical cyclones is expected to increase, but estimates are uncertain.

45. **Link to project activities.** The project has been subject to the World Bank's climate screening and the overall risk rating of the project is considered moderate. The risk rating to the development outcome of the project is considered low. It takes a proactive approach to mainstream Climate resilience and adaptation across its components, disbursement linked financing and capacity building activities.

46. The **project will contribute to reduced impacts of climate hazards by strengthening public investment management and making public investments more resilient to disasters and climate change.** The project will make the climate and disaster screening part of the project appraisal process and to develop a tool for climate and disaster screening (leveraging meteorological and disaster risk datasets and mapping) for NPD and other entities that are involved in project appraisal under sub-component 1.1.

47. **The project will develop and pilot test a policy and tool for green procurement is an integral part of sub-component 2.1 on Strengthening the procurement framework and development and roll-out of an e-Procurement system.** The green procurement policy and tool will ensure that the contracts awarded through e-Procurement system procure goods, services and works including low emission technologies with a reduced environmental impact throughout their life cycle.

48. **The development and testing of a policy on environmental audits by the Auditor-General under sub-component 3.2 will contribute to disaster risk reduction.** Environmental audits are voluntary in Sri Lanka while the financial audits are a part of the regulatory (legal) process. It is evident from the recent disasters that Sri Lanka has to significantly increase the environmental performance to reduce disaster risk. Capacity building of officials of NAOSL in environment audit and pilots on environment audit are proposed with the support of the project.

49. **Implementation support plan.** The project will require intensive technical and implementation support in the initial 2-3 years of the project especially to ground activities relating to the following:

- a) finalize the scope, functionality of the proposed information systems for Public Investment Management and Excise and to arrive at an informed decision of the nature, type and scope of the solution based on relevant international experiences and exposures
- b) Complete the training needs assessment in selected departments such as the Valuation Department, State Accounts Department, National Budget Department Attorney General's office and NAOSL to inform the nature and modality of trainings and identify other niche areas which are ripe for reforms such as Open Budget and gender budget; open contracting database, green procurement, climate disaster risk screening and modelling etc .
- c) Ensure that the basic project management oversight arrangements and implementation units are constituted and functioning, as intended.
- d) Selected rapid analytical and advisory work, as may be required in support of the proposed excise law/regulations, PFM law etc



50. This will require, in addition to the mandatory implementation support missions which will have participation of the core project team including technical team members, procurement and financial management specialists, 4-5 technical missions in response to specific and just in time technical assistance needs from specific global experts in the relevant domain. In doing so, the Bank will draw on the proposed EU funded Bank executed trust fund to bring in international expertise for providing technical advice and implementation support (international consultants, expertise from other governments which has successfully implemented similar reforms, and Bank technical specialists in the areas of reforms supported under PSEP project). These could also be consultants already contracted by the Bank to support PSEP in areas such as e-procurement, excise policy and law; the PFM law; and on the evaluation framework to provide continuity.