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PROJECT PERFORMANCE ASSESSMENT REPORT

COLOMBIA

**STRUCTURAL FISCAL ADJUSTMENT PROJECT
(TF-26673; FSLT-70920)**

**FIRST PROGRAMMATIC FISCAL AND INSTITUTIONAL
ADJUSTMENT LOAN
(LOAN NO. 7163-CO)**

**SECOND PROGRAMMATIC FISCAL AND INSTITUTIONAL
STRUCTURAL ADJUSTMENT LOAN
(LOAN NO. 72010-CO)**

**THIRD PROGRAMMATIC FISCAL AND INSTITUTIONAL
STRUCTURAL ADJUSTMENT LOAN
(TF-53133; FSLT-72800)**

April 22, 2008

*Country Evaluation and Regional Relations
Independent Evaluation Group (World Bank)*

Currency Equivalents (annual averages)

Currency Unit = Pesos (COP)

1996	US\$1.00	1,036.69
1997	US\$1.00	1,140.96
1998	US\$1.00	1,426.04
1999	US\$1.00	1,756.23
2000	US\$1.00	2,087.90
2001	US\$1.00	2,299.63
2002	US\$1.00	2,504.24
2003	US\$1.00	2,877.65
2004	US\$1.00	2,628.61
2005	US\$1.00	2,320.83
2006	US\$1.00	2,361.14

Abbreviations and Acronyms

CAS	Country Assistance Strategy
FIAL	Programmatic Fiscal and Institutional Adjustment Loan
GDP	Gross Domestic Product
ICR	Implementation Completion Report
IDB	Inter-American Development Bank
IEG	Independent Evaluation Group (Formerly OED)
IEGWB	Independent Evaluation Group (World Bank)
IMF	International Monetary Fund
ISS	Institute of Social Security
PPAR	Project Performance Assessment Report
RUT	Registro Único Fiscal
SFAL	Structural Fiscal Adjustment Program
VAT	Value Added Tax

Fiscal Year

Government: January 1 – December 31

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IEGWB Mission: Enhancing development effectiveness through excellence and independence in evaluation.

About this Report

The Independent Evaluation Group assesses the programs and activities of the World Bank for two purposes: first, to ensure the integrity of the Bank's self-evaluation process and to verify that the Bank's work is producing the expected results, and second, to help develop improved directions, policies, and procedures through the dissemination of lessons drawn from experience. As part of this work, IEGWB annually assesses about 25 percent of the Bank's lending operations through field work. In selecting operations for assessment, preference is given to those that are innovative, large, or complex; those that are relevant to upcoming studies or country evaluations; those for which Executive Directors or Bank management have requested assessments; and those that are likely to generate important lessons.

To prepare a Project Performance Assessment Report (PPAR), IEGWB staff examine project files and other documents, interview operational staff, visit the borrowing country to discuss the operation with the government, and other in-country stakeholders, and interview Bank staff and other donor agency staff both at headquarters and in local offices as appropriate.

Each PPAR is subject to internal IEGWB peer review, Panel review, and management approval. Once cleared internally, the PPAR is commented on by the responsible Bank department. IEGWB incorporates the comments as relevant. The completed PPAR is then sent to the borrower for review; the borrowers' comments are attached to the document that is sent to the Bank's Board of Executive Directors. After an assessment report has been sent to the Board, it is disclosed to the public.

About the IEGWB Rating System

IEGWB's use of multiple evaluation methods offers both rigor and a necessary level of flexibility to adapt to lending instrument, project design, or sectoral approach. IEGWB evaluators all apply the same basic method to arrive at their project ratings. Following is the definition and rating scale used for each evaluation criterion (additional information is available on the IEGWB website: <http://worldbank.org/ieg>).

Outcome: The extent to which the operation's major relevant objectives were achieved, or are expected to be achieved, efficiently. The rating has three dimensions: relevance, efficacy, and efficiency. *Relevance* includes relevance of objectives and relevance of design. Relevance of objectives is the extent to which the project's objectives are consistent with the country's current development priorities and with current Bank country and sectoral assistance strategies and corporate goals (expressed in Poverty Reduction Strategy Papers, Country Assistance Strategies, Sector Strategy Papers, Operational Policies). Relevance of design is the extent to which the project's design is consistent with the stated objectives. *Efficacy* is the extent to which the project's objectives were achieved, or are expected to be achieved, taking into account their relative importance. *Efficiency* is the extent to which the project achieved, or is expected to achieve, a return higher than the opportunity cost of capital and benefits at least cost compared to alternatives. The efficiency dimension generally is not applied to adjustment operations. *Possible ratings for Outcome:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Risk to Development Outcome: The risk, at the time of evaluation, that development outcomes (or expected outcomes) will not be maintained (or realized). *Possible ratings for Risk to Development Outcome:* High Significant, Moderate, Negligible to Low, Not Evaluable.

Bank Performance: The extent to which services provided by the Bank ensured quality at entry of the operation and supported effective implementation through appropriate supervision (including ensuring adequate transition arrangements for regular operation of supported activities after loan/credit closing, toward the achievement of development outcomes. The rating has two dimensions: quality at entry and quality of supervision. *Possible ratings for Bank Performance:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Borrower Performance: The extent to which the borrower (including the government and implementing agency or agencies) ensured quality of preparation and implementation, and complied with covenants and agreements, toward the achievement of development outcomes. The rating has two dimensions: government performance and implementing agency(ies) performance. *Possible ratings for Borrower Performance:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

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Principal Ratings

	<i>ICR*</i>	<i>ICR Review*</i>	<i>PPAR</i>
Structural Fiscal Adjustment Project			
Outcome	Satisfactory	Moderately Satisfactory	Moderately Unsatisfactory
Institutional Development Impact**	Modest	Modest	---
Sustainability	Likely	Non-evaluable	---
Risk to Development Outcome	---	---	High
Bank Performance	Satisfactory	Satisfactory	Moderately Unsatisfactory
Borrower Performance	Satisfactory	Satisfactory	Moderately Unsatisfactory

	<i>ICR*</i>	<i>ICR Review*</i>	<i>PPAR***</i>
First Programmatic Fiscal And Institutional Adjustment Loan			
Outcome	Satisfactory	Moderately Satisfactory	Moderately Unsatisfactory
Institutional Development Impact**	Substantial	Modest	---
Sustainability	Likely	Likely	---
Risk to Development Outcome	---	---	High
Bank Performance	Satisfactory	Satisfactory	Moderately Unsatisfactory
Borrower Performance	Satisfactory	Satisfactory	Moderately Unsatisfactory

	<i>ICR*</i>	<i>ICR Review*</i>	<i>PPAR***</i>
Second Programmatic Fiscal And Institutional Adjustment Loan			
Outcome	Satisfactory	Moderately Satisfactory	Moderately Unsatisfactory
Institutional Development Impact**	Modest	Modest	---
Sustainability	Likely	Likely	---
Risk to Development Outcome	---	---	High
Bank Performance	Satisfactory	Satisfactory	Moderately Unsatisfactory
Borrower Performance	Satisfactory	Satisfactory	Moderately Unsatisfactory

	<i>ICR*</i>	<i>ICR Review*</i>	<i>PPAR***</i>
Third Programmatic Fiscal And Institutional Adjustment Loan			
Outcome	Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory
Institutional Development Impact**	Substantial	Modest	---
Sustainability	Likely	Likely	
Risk to Development Outcome	---	---	High
Bank Performance	Satisfactory	Unsatisfactory	Moderately Unsatisfactory
Borrower Performance	Satisfactory	Unsatisfactory	Moderately Unsatisfactory

* The Implementation Completion Report (ICR) is a self-evaluation by the responsible Bank department. The ICR Review is an intermediate IEGWB product that seeks to independently verify the findings of the ICR.

**As of July 1, 2006, Institutional Development Impact is assessed as part of the Outcome rating.

***As of July 1, 2006, Sustainability has been replaced by Risk to Development Outcome. As the scales are different, the ratings are not directly comparable.

Key Staff Responsible

<i>Project</i>	<i>Task Manager/Leader</i>	<i>Sector Manager/ Sector Director</i>	<i>Country Director</i>
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Preface

This is the Project Performance Assessment Report (PPAR) for four structural adjustment lending operations to Colombia from 2001 to 2005:

The **Structural Fiscal Adjustment Loan** (P073572, TF-26673; FSLT-70920) was approved December 18, 2001 for \$US400 million equivalent. The first tranche amounting to \$US160 million was released December 20, 2001 and the second tranche of \$US180 million equivalent was released October 18, 2002, almost seven months from the planned March 31, 2002 release date. The third tranche of \$US60 million equivalent was finally released on February 11, 2003 and the project closed on February 21, 2003 with a delay of two months.

The **First Programmatic Fiscal and Institutional Adjustment Loan** (P080831; L/C 7163-CO) was approved on March 18, 2003 and released on March 20, 2003 in the amount of \$US300 million. The loan was closed on April 30, 2003.

The **Second Programmatic Fiscal and Institutional Adjustment Loan** (P083905; L/C 72010) in the amount of \$US150 million was approved on November 20, 2003 and became effective on November 24, 2003. The loan closed on the original date of February 25, 2004 and was fully disbursed.

The **Third Programmatic Fiscal and Institutional Adjustment Loan** (P084762; TF-53133; FSLT-72800) was approved March 22, 2005 and became effective on April 26, 2005. The loan was fully disbursed amounting to \$US100 million and closed based on the original date of June 30, 2005.

This PPAR is based on relevant Bank and Fund documents and on interviews with Bank staff. An Independent Evaluation Group (IEG) mission visited Colombia in October 2006 to discuss performance with officials who implemented the projects, representative donors, and staff of the Bank resident mission. Their cooperation and assistance in preparing the report is gratefully acknowledged.

Comments from the Bank's Regional Management have been incorporated in the report. The PPAR was also sent to the Government of Colombia whose comments was received last April 24, 2008 and is included in Annex C.

This report was prepared by Mr. Manuel Hinds (consultant), under the supervision of Ms. Helena Tang (Task Manager). Mr. Roderick de Asis provided research assistance and administrative support.

Summary

1. Attached is the Project Performance Assessment Report (PPAR) on four loans to the Republic of Colombia: the Structural Fiscal Loan (SFAL) for US\$400 and a programmatic series of three loans pertaining to the Fiscal Adjustment Loan (FIAL) Program, which was intended to add up to US\$900 million in four loans but eventually added up to US\$550 million in three loans. The four operations were part of the Bank effort to help the Republic of Colombia to attain fiscal sustainability in the long term. It is for this reason that they are reviewed in the same report.
2. The Colombian fiscal situation deteriorated sharply during the mid-1990s after having been managed reasonably well for several decades. As the fiscal deficit increased to levels of over 3 percent of GDP, the total gross stock of public debt reached 50 percent of Gross Domestic Product (GDP) by 2000, almost double the level in the early 1990s. A financial sector crisis then forced the government to issue more debt to re-capitalize the ailing financial institutions. In those years, it seemed that the country was on an unsustainable fiscal path.
3. In 1999, the then incoming Pastrana administration formulated a three-year stabilization program, supported by the IMF, and requested that the Bank take the lead in identifying and supporting the implementation of key structural reforms to help bring Colombia's fiscal accounts onto a sustainable path in the medium- and long-term. The Bank responded with the Structural Fiscal Adjustment Loan (SFAL).
4. The fiscal situation did not improve during the implementation of the SFAL. When the Uribe Administration took power in 2002, it devised a new program to deal with the fiscal problems and requested help from the Bank. This led to the design of the FIAL programmatic series. According to the program document presented to the Board of Directors in February 2003, "the series would support short- and medium-term reforms with twofold objectives: first, to help attain the substantial fiscal adjustment required to ensure macroeconomic stability and ease the significant fiscal rigidities that make the implementation of public policy extremely difficult; and second, to improve the provision of public services and establish the institutional basis for higher efficiency and accountability in public expenditures". The series was planned as four single-tranche loans, amounting to about US\$900 million in total. Decisions about whether and when the subsequent loans would go forward depended on the progress of the reform program. The Government cancelled the fourth FIAL before it was designed.
5. The performance of the Colombian economy improved drastically almost as soon as the first FIAL was approved, largely because the country experienced a significantly positive turn in the terms of trade (mainly through the increase in oil prices). The improved overall economic performance of the country had a favorable impact on the fiscal situation through several channels—including the increase in the royalties received by the government from its oil exploitation facilities; the buoyancy of the tax system, which tended to collect more with the same effort in good times than in bad times; and the reduction of the burden of the dollar-denominated debt that resulted from the appreciation of the peso which accompanied the improvement in the terms of trade.
6. The crucial question when evaluating the performance of the fiscal operations in Colombia is whether (and to what extent) the fiscal condition of the country improved

independently of the improved overall economic performance of the country. Stated in another way, the question is whether a reversal of the exogenous conditions since the early 2000s would not have resulted in a fiscal crisis similar to the one which prompted the design of the fiscal operations. These questions cannot be answered in a definitive way. Yet, it is possible to look at the different aspects of fiscal performance to ascertain whether they are likely to be sustainable if the exogenous variables that influence the Colombian economy so deeply were to deteriorate.

7. The first objective of the operation which was to help the borrower improve the underlying fiscal situation—was not accomplished. Although the deficit of the combined public sector went down from 3.2 percent in 2001 to 1.5 percent in 2006, most, if not all, of this improvement can be traced directly to the improved terms of trade condition, particularly to the increased income that the government received from the state-owned oil company (Ecopetrol). The underlying fiscal deficit situation did not improve since the beginning of the Bank-Support operations. The reduction of expenditure rigidities that negatively affect the fiscal system was not accomplished, either. In fact, the rigidity in the expenditure structure worsened during the implementation of the loans—in part as a result of measures that were taken under the loans.

8. The second objective of the operation was to help the borrower improve the provision of public services and establishing the institutional basis for higher efficiency and accountability in public expenditures. Some satisfactory results were achieved, but the overall outcomes were mixed.

9. The ratings presented in the report are lower than those in the ICR Review for earlier outcomes, and Bank and borrower performance. The ICRs rated the three areas of all the operations satisfactory. This PPAR considers that it would not be appropriate to rate as satisfactory a series of operations that failed to meet its main objectives and, in some cases, established conditions that contradicted the achievement of objectives. For the SFAL and the FIAL series, this PPAR rates all the three dimensions moderately unsatisfactory.

10. The main lessons learned from this review are:

- First, as noted in IEG’s ICR Review of FIAL III, project design needs to be clearly aligned with its development objectives in order to attain the latter. Even if the structural deficit of the central administration is “highly sensitive and political” as the ICR states, the magnitudes of these structural rigidities were such that they must be addressed if progress is to be made in achieving the substantial fiscal adjustment that is required for sustained macroeconomic stability.
- Second, loans with large numbers of objectives and conditions, and involving too many institutions relative to the management capacity of the Government and the Bank itself, overtax the implementation capacity of both the Bank and the borrower and result in poor execution.
- Third, the inclusion of objectives of widely different levels of priority and weak connection with the ultimate goals of the operations tends to obscure the degree of attainment of the latter.
- Fourth, success depends on the borrower’s ownership of the objectives of the loan.

Cheryl W. Gray
Acting Director-General
Evaluation

Introduction

11. This is the Project Performance Assessment Report (PPAR) of four loans extended to Colombia to help the government improve its fiscal performance and its institutional efficiency: the Structural Fiscal Adjustment Program (SFAL), and a series of three loans called the Programmatic Fiscal and Institutional Adjustment Loans, I to III (FIALS). Although the SFAL was an independent operation, it served as a stepping-stone for the design of the more ambitious program that framed the FIAL series. For this reason, this report evaluates the outcomes of three processes: the SFAL, the FIALS and the fiscal operations as a whole.

12. Both the SFAL and the FIAL program loans were extremely complex operations, with multiple and quite disparate objectives. These objectives differed in terms of their subject matter, the institutions involved, and their relative importance. Moreover, the conditions of these loans spread to several administratively unconnected institutions, and were drafted in many cases in a highly legalistic fashion that created chains of events passing from one loan to the next. For example, sequential operations included conditions that entailed, variously, the preparation, the presentation to Congress, the approval by Congress, and the regulation of different laws. In some instances, these chains were interrupted by the failure of Congress to do what the program intended it to do, which prompted the re-definition of conditions in several areas for the FIAL operating at the time and those following it. Eventually, the government decided that the problem of defining and redefining these multiple objectives, and the burden of tracking them through scores of institutions, was too taxing for the expected benefits and cancelled the fourth FIAL before it was designed.

13. The complexity of the loans poses a problem for their evaluation, too. This may become too mechanical and disjointed if it focuses too closely on the disparate conditions of the loans, to the point of becoming almost unreadable in the discussion of the laws (identified with numbers) that should have been drafted, proposed, approved or regulated in each of the versions of the FIALS. To address this problem, this PPAR takes a more general view: (a) looking at the FIALS as one single operation; and (b) focusing on the general objectives of the operations and evaluating the degree to which they were attained and the extent of the Bank's contribution to such attainment. Since each of the FIALS contained two components, 10 sub-components and 4 to 5 activities per sub-component, tracking them would entail reviewing 30 sub-components and 150 activities for these loans. Of course, the discussion cannot obviate the details of the operations, but the emphasis is on the forest, not the trees; on the overall path, not on each of its stations. A detailed description of the operations and a chronicle of the evolution of each of their components, sub-components and conditions is contained in the loans' ICRs. The IEG mission found this description satisfactory.

14. All the issues directly related with the attainment of the ultimate objective of the operations—improving fiscal performance—are discussed in one chapter (chapter 4). These issues are the outcomes of public debt management in the SFAL as well as the overall fiscal commitment in the FIAL loans, and the macroeconomic framework in both the SFAL and the FIAL loans.

15. Accordingly, the report contains five chapters and one statistical annex. Chapter 1 summarizes the economic background of the fiscal operations, from the approval of the SFAL to late 2006, one year after the closure of the FIAL series. Chapters 2 and 3 discuss the SFAL and the FIAL series in detail. Chapter 4 deals with the fundamental objective of the fiscal operations as a whole: improving fiscal performance. Chapter 5 discusses the lessons that can be extracted from these operations.

16. *Note on ratings.* This report rates highly unsatisfactory those components or activities that had outcomes that directly contradicted the objectives of the rated loans, by outcome or by design. For example, it rates highly unsatisfactory the outcome of a component of the SFAL which aimed at reducing current and general expenditures by 4 and 19 percent, respectively, in real terms, but resulted instead in an increase in those expenditures by 4 and 16 percent, respectively, also in real terms. Also, the report rates highly unsatisfactory the components that aimed at attaining goals that contradicted the objectives of the loans. These included two components, one in the SFAL and one in the FIALs, which increased the rigidity of the fiscal system by design, although reducing such rigidity was one of the main objectives of the loans. Another example is the structural reform of taxes, which actually increased the distortions that the loans had aimed at ameliorating. The report rates unsatisfactory those components that did not meet their objectives but did not contradict the objectives of the loan in their design or their outcomes.

1. The Economic Background of the Fiscal Operations

A. The Economic Environment

1.1 The Colombian fiscal situation deteriorated sharply during the mid-1990s after having been managed reasonably well for several decades. During the 1990s, central government expenditures grew from 9.3 to 20.1 percent of Gross Domestic Product (GDP) while revenues increased much less, from 11.0 to 13.3 percent of GDP, notwithstanding at least eight tax reforms that the government enacted during the period. As a result, total gross stock of public debt reached 50 percent of GDP by 2000, almost double the level in the early 1990s. The situation worsened with the recession that unfolded in 1998-99, which resulted in the first contraction of real GDP in over seventy years (real GDP fell by 3.7 percent in 1999 and remained below its 1998 level until 2001). A financial sector crisis exploded at that time which, though mainly affecting the state-owned banks, forced the government to issue more debt to re-capitalize the ailing institutions. In those years, it seemed that the country was on an unsustainable fiscal path.

1.2 In 1999, the then incoming Pastrana administration formulated a three-year stabilization program and requested support from the Bank to deal with the financial crisis (the program was also supported by an IMF Extended Fund Facility (EFF). The Bank responded with the Financial Sector Adjustment Loan (EUR 482 million) approved in November 1999. In 2000, the government requested that the Bank take the lead in identifying and supporting the implementation of key structural reforms to: (a) complement the stabilization effort under the IMF program; and (b) help bring Colombia's fiscal accounts onto a sustainable path in the medium- and long-term. The Bank responded with the Structural Fiscal Adjustment Loan (SFAL).

1.3 The downturn had revealed critical structural weaknesses in the government accounts—notably, the encroachment of entitlements in favor of politically powerful sectors, unbridled sub-national spending, the deterioration in quantity and quality of social services, and the substitution of current for capital expenditures. The SFAL focused its objectives and conditionality on these issues.

1.4 As discussed in more detail in chapter 2, the fiscal situation did not improve during the implementation of the SFAL. The fiscal deficit actually increased substantially, from 3.5 percent to 4.2 percent of GDP. Also, the substitution of current for capital expenditures continued unabated—current expenditures expanded by one percent of GDP while capital expenditures declined by 0.6 percent of GDP. Moreover, the transfers to local governments remained a crucial problem, the pension liabilities remained a heavy burden on the government, and the efficiency of social security did not improve.

1.5 As the fiscal situation deteriorated during the implementation of the SFAL, fiscal issues became more central to the government's and the Bank's programs. The 2002 Country Assistance Strategy (CAS) included macro-fiscal adjustment as one of the activities that needed to be carried out to meet one of the main CAS objectives—

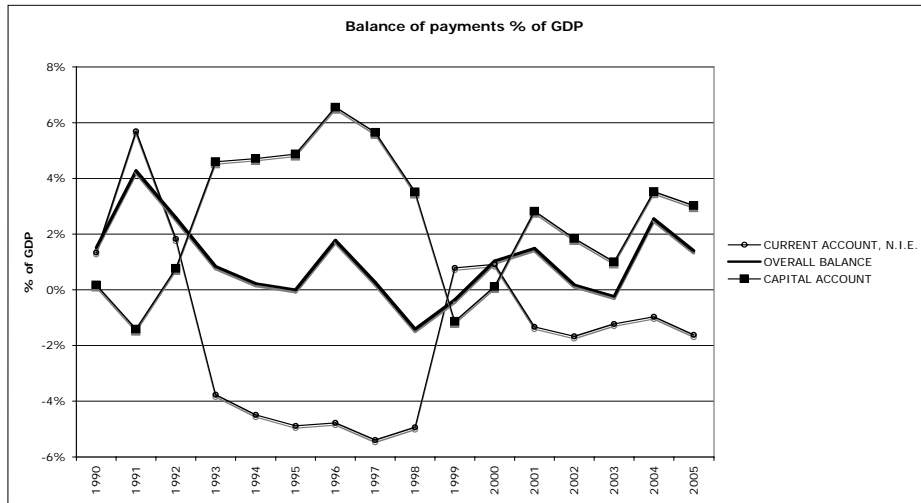
achieving fast and sustainable growth. The CAS listed actions on three fronts as a means to attain this objective: a major reduction in the size of the state, a “growth-friendly” tax reform, and better debt management. It was in this context that the opportunity to design and implement a programmatic series of loans presented itself.

1.6 The Uribe Administration, which took power in 2002, devised a new program to deal with the fiscal problems and requested help from the Bank. This led to the design of the FIAL programmatic series of loans. According to the program document presented to the Board of Directors in February 2003, “the series would support short- and medium-term reforms with two-fold objectives: first, to help attain the substantial fiscal adjustment required to ensure macroeconomic stability and ease the significant fiscal rigidities that make the implementation of public policy extremely difficult; and second, to improve the provision of public services and establish the institutional basis for higher efficiency and accountability in public expenditure. The program would consist of four single-tranche loans, adding to a notional amount of US\$900 million in total. Decisions about whether and when the subsequent loans would go forward will depend on the progress of the reform program.”

1.7 The performance of the Colombian economy improved drastically almost as soon as the FIALs were approved, mainly because several of the exogenous factors that had deteriorated during the crisis turned around and improved remarkably after 2002. These exogenous factors were the following.

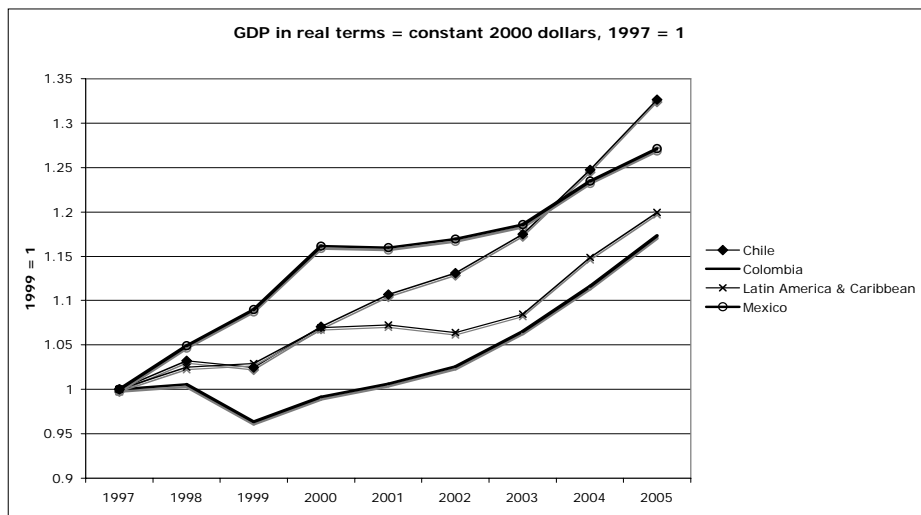
- The international prices of commodities, which had declined rapidly in the late 1990s and early 2000s, improved rapidly after 2002, leading to a rapid increase in exports, particularly of oil.
- The international crisis of 1997-98 eventually faded away, reversing the dramatic fall in capital inflows that had taken place in the previous years.
- As the current account improved and capital inflows returned to positive values, the peso appreciated in real and nominal terms, reducing the burden of the external debt denominated in dollars.

1.8 Figure 1 shows the behavior of the balance of payments before, during, and after the crisis. As is clear in the figure, the country was forced to adjust from 1996 to 1999 to a dramatic fall in capital inflows which was equivalent to about 8 percent of GDP. The adjustment had to be done through a compression of the current account of almost the same magnitude. This, however, was not sufficient, so that in 1998 and 1999 Colombia experienced overall balance of payments deficits, which led to losses in international reserves. This situation improved in the most recent years, as the prices of commodities (including oil) went up, and as capital inflows resumed, allowing Colombia to widen its current account deficits again. The combination of the current account deficits and the capital inflows has been such that it has allowed Colombia to run balance of payments surpluses, which in turn led to a rapid increase in international reserves.

Figure 1. Balance of Payments

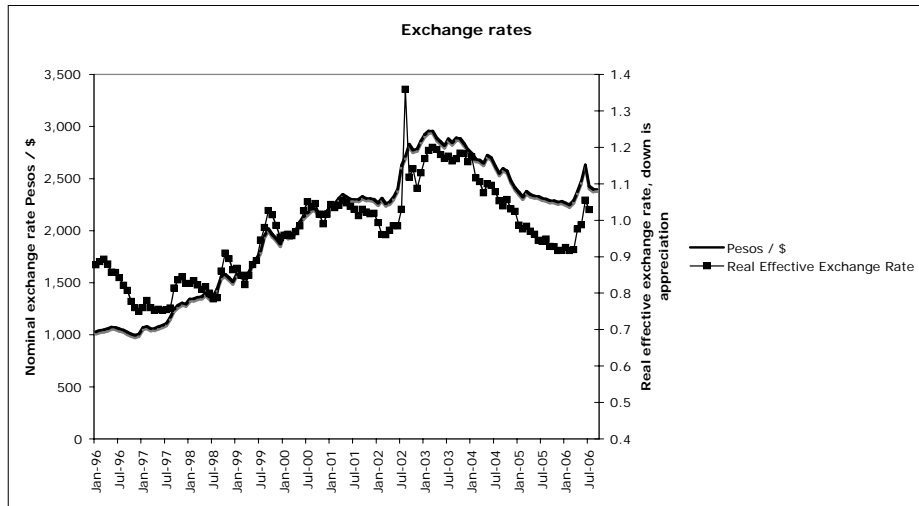
Source: *International Financial Statistics, IMF.*

1.9 Figure 2 shows how the economy reacted to these external events. After having declined in 1999, real GDP grew rapidly in the subsequent years, although by 2005 its level relative to 1997 still lagged behind that of the average in Latin America and well behind comparable leading countries such as Mexico and Chile.

Figure 2. GDP In Real Terms

Source: *World Development Indicators, World Bank.*

1.10 Figure 3 shows how the improvement in the balance of payments also led to a rapid appreciation of the currency that started in mid-2003. This in turn opened the space for domestic interest rates to fall, and reduced the burden of the external debt.

Figure 3. Exchange Rates

Source: *International Financial Statistics, IMF.*

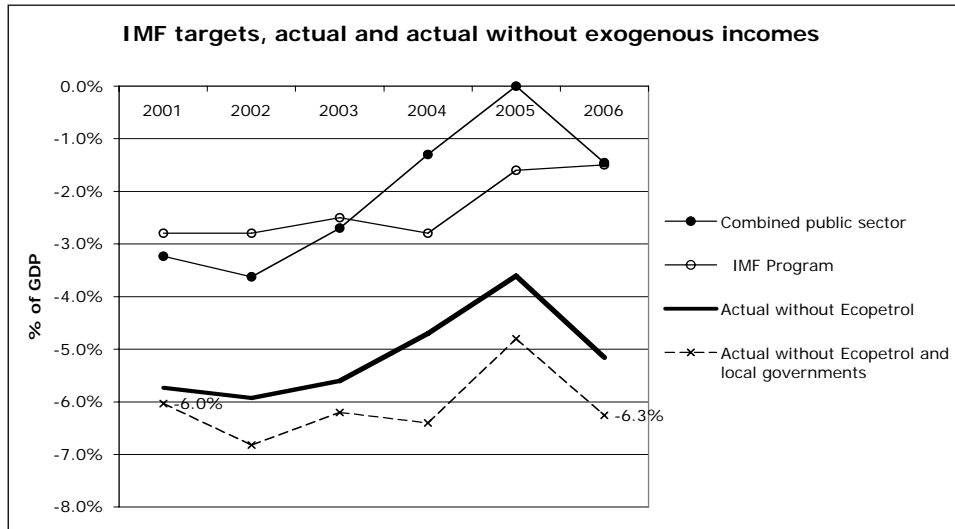
1.11 The improved overall economic performance of the country had a favorable impact on the fiscal situation through several channels—including the buoyancy of the tax system, which tends to collect more with the same effort in good times than in bad times; the reduction of the burden of the debt; and lower domestic and international interest rates, which further reduced the debt service.

B. Relations with the IMF

1.12 As noted before (see pp.1.2) the IMF supported the initial Pastrana 1999-2002 plan with an EFF in the amount of SDR1.957 billion (approximately US\$2.7 billion). A Stand-By Arrangement (SBA) in the amount of SDR 1.55 billion followed this operation for a period of 24 months from December 2002. Then, the IMF approved a new precautionary SBA (not intended to be disbursed) in the amount of SDR405 million. The country exited from formal Fund support at the end of this arrangement.

1.13 Colombia experienced difficulties in meeting IMF conditions under the EFF as the fiscal situation kept on deteriorating up to the end of 2002 (while the SFAL was in effect). Then, as the external economic conditions of the country rapidly improved, Colombia was able to meet practically all the fiscal conditions of the two SBAs that went from the end of 2002 to the end of 2006. Figure 4 shows how the fiscal performance of the broadest definition of government (the combined public sector) consistently equaled or exceeded IMF targets from 2003 onwards. This was fully satisfactory from the point of view of the IMF. The figure, however, also shows that most of the improvement was due to: (a) increased contributions of Ecopetrol, the state-owned oil company, which experienced a boom in those years as a result of the high oil prices; and (b) limited implementation capacity of the local and regional governments, which produced surpluses in these years. Without Ecopetrol, the 2006 deficit would have been 5.2 percent of GDP, just a little lower than the 2001 deficit that motivated the operations; if the surpluses of the local governments were excluded, the 2006 fiscal deficit was worse than that of 2001.

Figure 4. Fiscal Balances of Combined Public Sector, Targets and Actual Outcomes



Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

C. The Main Issues

1.14 Notwithstanding IMF satisfaction with the fiscal outcomes from end-2002 to end-2006 (which is in line with the short-term nature of IMF activities), the high reliance of the fiscal outcomes on the profits of Ecopetrol and the circumstantial surpluses produced by the local governments poses serious issues from the Bank's long-term point of view, as the purpose of the reviewed operations was precisely to improve the fiscal situation structurally. Without these two circumstantial events, the country would have had a deficit larger than that of 2001.

1.15 The high contribution of Ecopetrol's profits to the reduction of the combined public sector deficit raises particular concerns because they are likely to go down as the reserves of the company will be depleted in the near future unless the company invests heavily in further exploration. The resources for such investment would have to come from those that have been going to reduce the fiscal deficit. Alternatively, as analyzed in a recent paper by the IMF, the country could classify the company as commercially run and remove it from the country's financial indicators, targets and accounts. This, of course, would increase the measurement of the combined public sector deficit instantaneously.¹

1.16 These concerns are even more important because other exogenous factors also contributed to the improvement in the fiscal balance. As is very common for countries that depend on commodities, all macroeconomic variables improve when their prices increase. For instance, fiscal collections go up as a result of the economic boom

¹ See The Fiscal Risk of Public Enterprises: Analysis of Isagen and Ecopetrol, in Colombia Selected Issues, November 2006, IMF Country Report No. 06/401.

generated by the high commodity prices, and the currency appreciates which reduces domestic interest rates and the burden of the external debt. By the same token, a reversal in the behavior of these exogenous variables would lead to increased difficulty in collecting taxes; to an increase in the burden of the debt; and to higher interest rates, which would raise debt servicing needs.

1.17 Thus, the crucial question when evaluating the performance of fiscal operations in Colombia is whether (and to what extent) the fiscal condition of the country has improved independently of the improved overall economic performance of the country and of the windfall oil price boom—as was clearly the overall objective of the evaluated operations. In other words, the question is whether a reversal of the exogenous conditions that have improved since the early 2000s would not result in a fiscal crisis similar to the one that prompted the design of the fiscal operations.

1.18 These questions cannot be answered in a definitive way. Yet, it is possible to look at the different aspects of fiscal performance to ascertain whether they are likely to be sustainable if the exogenous variables that influence the Colombian economy so deeply were to deteriorate. The next three chapters deal with this issue: chapters 2 and 3 review the implementation of the fiscal loans, while chapter 4 examines the main changes in the fiscal situation of the country that took place from 2001 to 2005.

2. The Structural Fiscal Adjustment Loan

2.1 The 1999 Country Assistance Strategy Progress Report (CAS-PR) noted that the performance of the Colombian economy had deteriorated sharply during the two years since the presentation of the last full CAS, particularly in terms of economic growth and fiscal stability. Controlling the fiscal deficit was very difficult because of the substantial rigidities that existed in the fiscal system. Worst among them was the rigidity of the transfers to local and regional governments, which were fixed as a percent of fiscal revenues, reducing the government's ability to save part of those revenues. The sharp increase in the fiscal deficit that was taking place in those years was largely attributed to this rigidity. The fiscal situation negatively affected the CAS objectives in two crucial dimensions. First, the fiscal deficits generated substantial instability, which in turn affected the economy's ability to grow and allocate its resources efficiently. Second, the composition of public expenditure was shifting, with current expenditures increasing while public sector investment was declining fast. As a result, restoring the fiscal balance was deemed crucial for the success of Colombia's efforts to recover growth and reduce poverty. This set the policy framework for the SFAL, which would help the Colombian government to reduce the fiscal deficit by reducing the rigidity of the transfers to the local and regional governments, as well as by improving the financial management of some educational and social security institutions.

A. The Loan

2.2 The SFAL was a US\$400 million fixed-spread loan, with a maturity of 13.5 years. The loan was programmed for disbursements in three tranches over a 14-month period, with the disbursement of each tranche being tied to the implementation of the fiscal reform program. It was approved on November 16, 2001. The following subsections discuss the attainment of each of its components.

B. Objectives

2.3 According to the Report and Recommendation of the President, the SFAL "was the Bank's response to the government's demonstrated commitment to reaching an inflection point in Colombia's fiscal accounts path, an essential first step toward achieving full fiscal sustainability, economic growth, and poverty reduction." The program supported by the SFAL aimed at improving the country's fiscal outlook by focusing on a core set of policies. This policy package involved:

- **Macroeconomic framework.** Improve the country's macroeconomic situation and particularly the fiscal situation.
- **Containment of expenditures.** Help the fiscal adjustment by reducing current and general expenditures in real terms.
- **Transfers to local governments.** Rationalize the system of transfers to local governments, and impose more market-driven and more binding budget constraints on their finances;
- **Public health efficiency.** Establish mechanisms to arrest the exploding cost of inefficiency in the provision of public health services;

- **Pension liabilities.** Halt the accumulation of pension-related contingent liabilities;
- **ISS Reform.** Advance the reorganization of the Social Security Institution to make it financially viable; and
- **Public Debt.** Set up a better system for managing public debt.
- **Education.** Carry out some institutional improvements in the provision of education at the local and regional levels.

C. Components

2.4 The loan had seven components to meet these objectives. The following subsections review them briefly.

Macroeconomic Framework

2.5 As shown in Table 1, the fiscal situation deteriorated during the implementation of the SFAL: (a) the fiscal deficit increased from 3.5 percent to 4.2 percent of GDP; and (b) current expenditures continued to increase while capital expenditures continued to fall, both as a percent of GDP.

Table 1. Change in the Balance of the Non-Financial Public Sector, 2001-2002 (percent of GDP)

	2001	2002	Difference 2002-01
Total revenue	29.5%	29.5%	0.0%
Current revenue	29.5%	29.5%	0.0%
Tax revenue	19.2%	19.1%	-0.1%
Total expenditure and net lending	33.2%	33.5%	0.3%
Current expenditure	24.9%	25.9%	1.0%
Capital expenditure	8.2%	7.6%	-0.6%
Net lending	0.1%	0.1%	0.0%
Statistical discrepancy	0.2%	-0.1%	-0.3%
Non-financial public sector balance	-3.5%	-4.2%	-0.7%

Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

2.6 The fiscal balance was substantially worse than in 2001, when the loan was approved to improve it, and much worse than the targets established in the Bank and the IMF programs. While the Bank did not establish an explicit fiscal deficit target in the conditionality of the loan, paragraph 53 referred to a set of projections contained in Table 1 of the President's Report as the expected outcomes of the program that the loan was to support. In that table, the target fiscal deficit was 3.1 percent of GDP. The target under the then existing IMF's EFF was 2.8 percent. This means that the fiscal deficit in 2002 was 1.1 percent of GDP worse than the expected outcome contained in the Bank's President's Report, 1.4 percent of GDP worse than the IMF's target, and 0.7 percent of GDP worse than in 2001.

2.7 The ICR rated this component as satisfactory, justifying this rating with the following arguments: “During the program period Colombia encountered several economic challenges. It faced issues of contagion resulting from economic problems in Venezuela, the largest market for Colombia's nontraditional exports; the worsening of market sentiment toward Latin America; and slow economic recovery in the United States, Colombia's main trading partner. Internally it faced increasing security costs at the same time as it was undergoing a political transition. In light of these issues and its efforts to maintain a stable economy, despite a significant deterioration in its fiscal deficit in 2002, the macroeconomic framework is evaluated as having been consistent with the objectives of the program.”

2.8 IEG's ICR review concurred with the ICR in rating this aspect of the loan “satisfactory”, noting that the rate of growth of the economy had improved, that inflation had declined and that “the fiscal deficit grew in 2002, contrary to the program's objectives, but then it fell in 2003.”

2.9 There were indeed improvements (albeit rather modest ones) in the rate of growth of the economy (which rose from 1.5 to 1.9 percent) and inflation (which fell from 7.9 to 6.4 percent) between 2001 and 2002. Despite these improvements, tax collection fell by 0.1 percent of GDP while current expenditures increased by one percent of GDP, worsening the fiscal deficit, which was a problem that the loan had aimed at ameliorating. Moreover, while the deficit improved one year later, in 2003, this happened under the FIAL program, reviewed in the next chapter and, as noted there, it did so mainly because the country's external conditions improved.

2.10 This report rates the achievement of the objective of this component negligible, as the government did not only fail to advance in the attainment of its objectives but in fact experienced a setback. Setbacks can be understandable but cannot be considered satisfactory. In terms of achievement of objectives, the report rates the component negligible.

Public Sector Reform (Expenditure Control)

2.11 This component was aimed at addressing the lack of control over government expenditures (rather than public sector reform in general), which was one of the main causes of the fiscal deterioration that prevailed at the time of the SFAL design. Under the loan, the government undertook commitments to reduce and rationalize such spending in two main categories: current and general expenditures.

2.12 **Current expenditures.** The government committed itself to reduce these expenditures by more than 4 percent in real terms from 2001 to 2002 in the approved budget for central government current expenditure. The approved budget complied with this restriction (as did spending levels at the time of the second tranche release in 2002). However, final spending by year-end was a 4 percent increase over FY2001 spending levels in real terms. Thus, the difference between the commitment and the outcome was 8 percent in real terms.

2.13 **General expenditures.** The commitment was to reduce these expenditures by 19 percent in real terms. As with current expenditures, the government reduced the

budgetary appropriations by the agreed amount. However, also as in the case of current expenditures, these expenditures actually increased during the implementation of the budget, by 16 percent in real terms, making for a difference between goal and achievement of 35 percent in real terms.

2.14 The ICR rated this component as moderately satisfactory and the IEG's ICR Review unsatisfactory. This report rates the outcome of this component as highly unsatisfactory because, rather than reducing the current and the general expenditures in real terms, the government increased them by the amounts it was supposed to reduce them. In terms of achievement of objectives, the report rates the component as negligible.

Intergovernmental Fiscal Relations

2.15 Intergovernmental fiscal relations became a serious problem during the 1990s. According to the 1991 Constitution, the central administration should transfer some of its revenues to territorial governments to support spending, especially on health and education. The constitution stated that the transfers should rise in line with the growth in current revenues, worsening a fiscal rigidity problem that was already substantial in Colombia. The problem, however, went beyond rigidity. The local and regional governments overspent and asked for complementary funds, which were routinely granted even if they were substantial.

2.16 The loan objectives in this respect were the following.

- **Intergovernmental transfers.** Fix in real terms the rate of growth of fiscal transfers to the regional and local governments for 2002 and thereafter.
- **Local taxation.** Reform the tax system of territorial entities (Estatuto de Ingresos Territoriales) to increase sub-national tax revenues by more than 20 percent in its first year of application.
- **Local and regional borrowing.** Issue and implement a decree to regulate debt and borrowing of territorial entities that would contribute to halting unsustainable borrowing, limiting bailouts, and eliminating discretion in the treatment of debt.

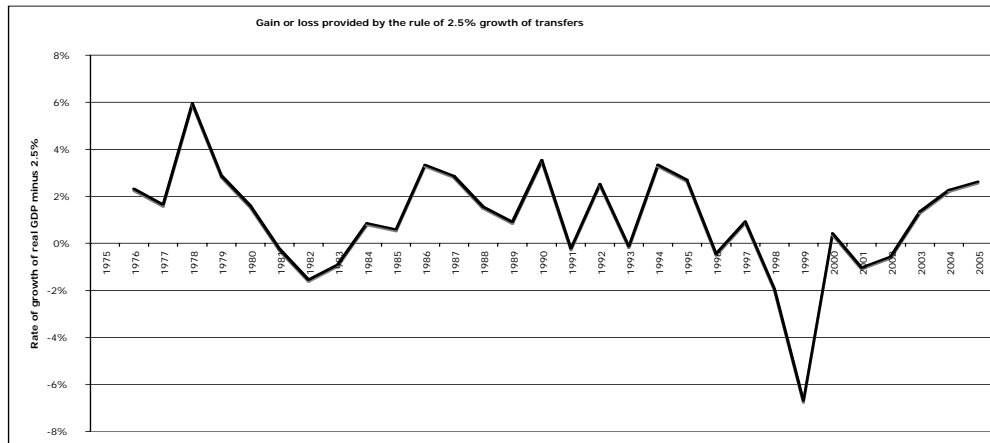
2.17 **Intergovernmental transfers.** This objective was attained. A constitutional reform created what was called a "transition period" from 2002 to 2008. During that period, transfers in real terms would grow at 2 percent per year from 2002 to 2005, and at 2.5 percent per year from 2006 to 2008. According to the amendment, transfers would increase in line with the central administration's current revenue again from 2009 on.

2.18 The reform, however, worsened the rigidity of the fiscal budget. Prior to the reform, these transfers increased and decreased with revenues. With the new provision, they would always grow at a fixed rate during the period of effectiveness of the Constitutional reform. Thus, rigidity would remain a crucial problem. Only one year later, the FIAL documents would call rigidity "the key constraint to effective public

policy”.² In fact, fiscal flexibility was sacrificed in exchange for: (a) predictability (the real rate of growth of transfers was both a floor and a ceiling); and (b) a potential long-term gain that would be obtained by fixing the rate of growth of transfers at a rate lower than the average rate of growth of fiscal revenues or GDP.

2.19 Over the last 30 years, the rate of growth of GDP did tend to be higher than 2.5 percent—it averaged 3.5 percent (Figure 5). If this average rate were to be maintained in the future, the rule would result in a reduction in the share of GDP being transferred to the territorial authorities. Yet, there are three problems with this reasoning. First, the rigidity could cause serious fiscal problems in the years when GDP grows by less than 2.5 percent. There were 10 such years since 1975 and, in one of them (1999), the difference in the rates of growth was almost 7 percent. Being forced to increase transfers in a year of GDP decline would worsen the problems of fiscal adjustment, particularly in a country where fiscal rigidity is already a serious problem and where, by 2005, transfers had reached 4.9 percent of GDP, and about 40 percent of public expenditure was carried out at the decentralized level. Second, while over the last 30 years the economy’s rate of growth was higher than 2.5 percent, in the last 10 years it was only 2.2 percent, and if this average growth rate were to prevail in the future, the share of GDP transferred to territorial authorities would increase. In any case, establishing a fixed rate of growth for the transfers to the local and territorial entities clearly increased the rigidity of the system and created a problem that the Bank is now urging the government to remove. The 2005 Country Economic Memorandum identifies the growth of these transfers in real terms as one of the main fiscal problems and recommends keeping them constant to facilitate fiscal adjustment.³

Figure 5. Rate of Growth of GDP minus 2.5%



Source: *World Economic Indicators*, World Bank.

² Program document presented to the Executive Directors on the FIAL program, Report No. 25476-CO, page 7.

³ *Colombia Country Economic Memorandum, The Foundations for Competitiveness*, November 8, 2005, Report No. 32035-CO, pp. 127.

2.20 In actuality, the rates of growth of GDP and fiscal revenues had exceeded 2.5 percent in real terms since 2003, which had resulted in a decline in the ratio of local and regional transfers to GDP and to fiscal revenues since that year. The government is planning to propose to the National Assembly to turn the 2001 Constitutional reform permanent when its life ends in 2009.

2.21 In sum, the Constitutional reform that the FIAL supported helped to introduce order in the process of transfers, as fixing their rate of growth in real terms in practice eliminated the budget adjustments that were at the root of the still faster growth of these expenditures in the years prior to the reform. The problem is that the reform actually increased the system's rigidity: under the current Constitutional provision the government would not be able to stop or even reduce the real rate of growth of transfers if the country gets into a slump. If the situation that prevailed from 1998 to 2002 were to prevail again, the transfers to the local and regional governments would increase by 10.4 percent in real terms while GDP would have increased by only 2.0 percent over the 4 years. Given that one of the objectives of the loan was to reduce the rigidities of the Colombian fiscal system, and particularly their effect on the country's ability to adjust in critical circumstances, this was a highly unsatisfactory outcome. In terms of achievement of the objectives, the report rates the component negligible.

2.22 **Local taxation and debt.** The two other objectives of the intergovernmental fiscal relations component were attained: sub-national tax revenues increased by more than 20 percent, and debt management of territorial authorities has improved. In fact, as discussed later, the territorial authorities are in fiscal surplus nowadays, although to a large extent this is due to the lack of implementation capacity.

2.23 Although the government attained its stated objective, the reform increased the country's fiscal rigidity, an already severe problem, the solution of which became the main objective of the FIAL program. This report therefore rates this component as highly unsatisfactory. The achievement of objectives was negligible.

Health

2.24 The government's main commitments with respect to health services were to: (a) reduce inefficient supply-side subsidies; and (b) limit the fiscal costs to the national government while improving service. According to the matrix of policy actions of the loan, the Ministry of Health, the Department of National Planning, and the Ministry of Finance would define and approve a national public hospital restructuring policy and an implementation program for the next five years, and would begin the implementation of the first phase, including the selection of at least 10 departments. Additionally, the government would sign contracts with at least three sub-national governments to finance the restructuring of public hospitals.

2.25 Under the SFAL, the government implemented the National Hospital Restructuring Policy. The pilot phase of the program in 2002 covered more than 10 departments and 15 percent of the total hospital budget. The program included specific targets for cost reduction and productivity increases, which, according to the ICR, generated more than 5 percent in fiscal savings per month.

2.26 This report confirms the ICR rating of satisfactory for this component. The achievement of objectives was substantial.

Institute of Social Security (ISS) Reform

2.27 At the time of approval of the SFAL, the ISS was not financially viable. The government had initiated a restructuring plan for the health aspects of ISS, including negotiating with ISS unions about labor costs and benefits, and had implemented the first phase, including renegotiation of 50 percent or more of ISS's total outstanding debt to health service providers, and reduction of at least 30 percent of the waiting list for elective surgeries (as of June 30, 2001). The government and the ISS had reached an agreement to generate annual savings in ISS's total costs over a 10-year period which would, in the opinion of the Bank, make ISS financially and economically viable. The plan, however, did not work and the ISS remains as unviable as it was in 2001.

2.28 The ICR rated this component as unsatisfactory. This report confirms this rating. It rates the achievement of objectives negligible.

Pensions

2.29 The condition of Colombia's pension system constituted a major risk to fiscal sustainability over the medium and long term at the time of loan design. The pension system was technically insolvent and the annual imbalances in the public sector worker regimes were increasing. The estimated net present value of pension system liabilities amounted to about 200 percent of GDP in 2000—up from an estimated 150 percent of GDP in 1997. Moreover, the Treasury's transfers to finance the deficits for public sector worker regimes increased from about 0.8 percent of GDP in 1991 to 1.3 percent of GDP in 1995 and to 2.3 percent of GDP in 2000. The causes of the current pension system insolvency and liquidity problems included too-generous benefits, benefit guarantees, perverse incentives for reserve management, and a Constitutional Court ruling expanding pension benefits.

2.30 This component had three objectives:

- Improving social security system control through the creation of a new social security department; this is estimated to generate fiscal savings of around \$100 million in 2001.
- Concentrating transfers of the public sector pension regimes into a single agency which is estimated to generate savings of around \$10 million per month on average.
- Enacting a series of parametric reforms that would make the pension system more equitable and sustainable.

2.31 Regarding the first two objectives, the government created the Social Security Economic Regulation Agency (Dirección de Regulación Económica de la Seguridad Social, DRESS) to serve as a counterpart and advisor to the Ministry of Social Protection (Ministerio de Protección Social, MPS) in managing and tracking pension and social security expenditures. The activities of DRESS include the tracking, validation, and the calculation of actuarial pension benefits, and the pension payments of the National Public

Pension Fund (Fondo de Pensiones Públicas del Nivel Nacional, FOPEP). Ongoing controls and enhanced administration generated significant fiscal savings in the areas of pensions, health, and workers compensation (estimated at US\$300 million in 2001).

2.32 Regarding the third objective, the Congress also passed a pension reform law in December 2002. With these reforms in place, new entrants into the system will not generate increases in the actuarial deficit, although this deficit still exists and further reform or financing is required to overcome this. The government enacted further reforms after the closing of the loan. These reforms, enacted from 2002 to 2005, together with demographic trends, are expected to reduce payments of pension benefits by 1 percentage point of GDP by 2015.

2.33 This report concurs with the ICR in rating this component satisfactory. It rates the achievement of objectives substantial.

Public Debt

2.34 As noted in the Introduction to this report, the analysis of the overall fiscal commitment and public debt sustainability is contained in chapter 4 for the SFAL and the FIAL operations. Regarding the specific objectives of SFAL in this respect, the government would develop new portfolio and funding strategies, integrating fiscal projections with portfolio analysis, with the ultimate aim of reducing the central government's debt exposure. The government carried out these activities to the satisfaction of the Bank.

2.35 This report concurs with the ICR in rating this component satisfactory. It rates the achievement of objectives modest.

Education

2.36 With the passing of Law 715 of 2001, the government created a framework to certify the adequacy of management in the provision of education services at the local and regional levels. The law allowed all municipalities that are capitals of departments or have a population of more than 100,000 inhabitants to receive certification. These represented more than 40 percent of the country's school enrollment. Performance monitoring mechanisms were also established with these municipalities to monitor quality of service provision.

2.37 This report confirms the ICR rating, satisfactory. It rates the achievement of objectives modest.

Summary and Comparison with ICR And ICR Review Ratings

2.38 Table 2 summarizes the ratings of the components in this PPAR and compares them with those of the ICR and the IEG's ICR Review.

Table 2. Summary of Ratings for the SFAL by Component

COMPONENTS	ICR RATINGS	IEG REVIEW	PPAR RATINGS	REASONS FOR DISAGREEMENT
Macro framework	Satisfactory	Satisfactory	Highly Unsatisfactory	The fiscal deficit and the current expenditures, basic determinants of the macro framework, deteriorated sharply during the life of the loan
Containment of expenditures	Moderately Satisfactory	Unsatisfactory	Highly Unsatisfactory	Expenditures increased in real terms instead of declining, as was the loan's condition.
Transfers to local governments	Satisfactory	Satisfactory	Highly Unsatisfactory	The measure supported by the loan increased the rigidity of the fiscal system, which, according to the Bank and the IMF, was and is one of the worst fiscal problems.
Health efficiency	Satisfactory	Satisfactory	Satisfactory	
ISS Reform	Unsatisfactory	Unsatisfactory	Unsatisfactory	
Pensions	Satisfactory	Satisfactory	Satisfactory	
Public Debt	Satisfactory	Not rated	Satisfactory	
Education	Satisfactory	Satisfactory	Satisfactory	

Source: World Bank

D. Assessment of the Operation

2.39 **Quality at entry.** The quality at entry was deficient because the design of the loan introduced a budgetary rigidity (the rates of growth of the intergovernmental transfers in real terms) among the most important activities that it supported. Just one year later the Bank was branding budgetary rigidities as the worst obstacle to public policy making.

2.40 **Relevance.** The overall objectives of the operation were relevant to the problems of Colombia and fully consistent with the CAS, although the design of the operation, as noted above, served to worsen a key weakness of the fiscal system.

2.41 **Outcomes.** According to the ICR, “the SFAL assisted the government in two important ways. First, it helped the government to begin a process of slowing the growth of fiscal imbalances. The proceeds from the loan helped to reduce the cost of borrowing and to lengthen the debt maturity by providing a confidence-building signal to international markets, all of which gave the government fiscal space for protecting social sector expenditures and implementing difficult structural measures. Second, the SFAL promoted reforms in the provision of public services that improved incentive structures and provided substantial efficiency gains. As a result, the fiscal rigidities facing the Colombian government were reduced and the fiscal situation is gradually stabilizing—important first steps in putting Colombia on a sustainable path.”

2.42 This report does not take such a sanguine view of the operation. Certainly, several components of varying importance had satisfactory results. However, the government failed in two of the fundamental ones. First, it established a rule for intergovernmental transfers that increased fiscal rigidity, which only months later was identified by the FIAL program as one of the worst fiscal problems of the country. Second, it failed in the key stabilizing condition: reducing current expenditures by 4 percent and general expenditures by 15 percent (both in real terms). Rather than falling by the promised results, these expenditures increased by almost the same magnitudes in real terms. Moreover, the government was unable to reverse the trend in the composition of expenditures, which was increasing current expenditures at the expense of capital ones; in fact, current expenditures increased while the capital ones declined. As a result of all these factors, the outcomes contradicted the objectives of the loan and the overall fiscal situation worsened instead of improving.

2.43 Institutional development was substantial in pension reform but negligible in the rest of the operation. While pension reform was a crucial component of fiscal reform, its institutional development fell short of what was needed in the other areas of the loan to meet the loan objectives—to help the government take an essential first step toward achieving full fiscal sustainability, economic growth, and poverty reduction.

2.44 The ratings by component show that four of the eight had a satisfactory outcome. Yet, the components that had a more direct bearing on the ultimate objectives of the loan were rated highly unsatisfactory: (a) improving the fiscal balance by (b) reducing current and general expenditures in real terms and by (c) reducing the rigidity of the fiscal system. Since (a) the fiscal balance deteriorated while (b) current and general expenditures increased substantially in real terms and (c) fiscal rigidity increased, the rating of the operation on the basis of its most important objectives would be highly unsatisfactory. Given that the project included other components and that four of them were completed satisfactorily, this report rates the SFAL moderately unsatisfactory.

2.45 **Risk to development outcome.** The loan did not meet its objectives during its lifetime. It is not likely to meet them afterwards because its risk to development outcome is substantial in four dimensions. First, given that the deficit worsened rather than improved, the fiscal measures supported by the loan lacked viability in the long term. Second, the fiscal deterioration that took place during the life of the loan showed a low level of ownership and commitment by the government to the objectives of the loan. Third, the institutional setting did not improve in terms of its ability to support the loan objectives during and after loan implementation. Fourth, as discussed in Chapter 4, the capacity of the country to respond effectively to a worsening of economic conditions, such as those that originated the loan, did not improve as a result of the loan. For these reasons this report rates the risk to development high.

2.46 **Bank performance.** The supervision of the loan was satisfactory in the sense that the staff did its best to help the borrower to meet the objectives of the loan. This did not fully compensate for the fact that the design of the loan, which included as part of the conditionality a reform that worsened one of the main fiscal problems of the country. For this reason the Bank performance is rated moderately unsatisfactory.

2.47 **Borrower performance.** Given the poor performance on reducing expenditures, a central objective in improving the fiscal outlook, the borrower performance is rated moderately unsatisfactory.

E. Comparison with Ratings of ICR and ICR Reviews

2.48 Table 3 summarizes the differences between the ratings of the ICR, IEG's ICR Review and this PPAR, as well as the reasons for disagreement.

Table 3. Summary of Ratings for the SFAL Program

	ICR RATINGS	IEG REVIEW	PPAR	REASONS FOR DISAGREEMENT
Outcome	Satisfactory	Moderately satisfactory	Moderately Unsatisfactory	The fiscal situation worsened during the implementation of the loan for reasons attributable to the borrower. The government aimed at reducing real current expenditures by 4 percent but instead they increased by 4 percent, making for an 8 percent difference with the target. General expenditures were to be reduced by 19 percent but instead they increased by 16 percent, both figures in real terms. Moreover, the loan increased fiscal rigidity of the country.
Institutional development	Modest	Modest	Evaluation included in risk to development, which was rated high	
Sustainability	Likely	Unlikely	Evaluation included in risk to development, which was rated high	
Risk to development outcome			High	The capacity of the country to respond effectively to a worsening of the economic conditions, such as the one that originated the loan, did not improve as a result of the loan.
Bank performance	Satisfactory	Satisfactory	Moderately Unsatisfactory	The Bank included as one of the conditions of the loan a reform that worsened one of the main problems of the system.
Borrower performance	Satisfactory	Satisfactory	Moderately Unsatisfactory	The borrower had a satisfactory performance in 4 of the 8 components. Yet, Its fiscal situation deteriorated substantially and the loan worsened one of the main fiscal problems of the country: expenditures rigidity.
Quality of ICR		Unsatisfactory	Not rated	

Source: World Bank

3. The Programmatic Fiscal and Institutional Adjustment Loan Program

A. The Program and its Objectives

3.1 The Board of Directors approved the FIAL program on February 2003 to support the program of reforms proposed by the new Uribe administration. The program would support a series of up to four loans, with a notional envelope of up to US\$900 million in total. The loans were fully consistent with the 2003 CAS. In reality, the program supported only three loans, for a total of US\$550 million (US\$300 million equivalent for FIAL I, approved on March 18, 2003; US\$150 million equivalent for FIAL II, approved on November 24, 2003; and US\$100 million equivalent for FIAL III, approved on April 23, 2005). The first loan was released on March 20, 2003; the second on November 24, 2003 and the third on April 25, 2005. The last loan was closed on June 30, 2005.

3.2 The Letter of Development Policy described the overall objectives of the program as twofold: “first, to promote reforms addressing fiscal rigidities necessary to attain the substantial fiscal adjustment underlying sustainable macroeconomic stability; and second, to improve the provision of public services and establish the institutional basis for higher efficiency and accountability in public expenditure. The emphasis of the reform program would gradually shift, from tax and fiscal responsibility at the beginning, to expenditure and public sector reform towards the second and third years of the program.”

3.3 Regarding the first objective, the same letter stated that: “The fundamental issue that constrains the implementation of financial policy in Colombia is the inability of the government to access the necessary budgetary resources to attend policy priorities. Fiscal rigidities, in the broad sense, incorporate a number of concepts that cover areas such as tax policy and administration, budget management, civil service, judicial decisions, and administrative processes such as public procurement and contracting and asset management. The common thread that connects these diverse areas is that they all generate an entrenched expenditure that is difficult to reduce, produce excessive costs derived from fundamental inefficiencies, and/or prevent a revenue source from reaching its full potential.”

3.4 Among the most important types of fiscal rigidities, the letter mentions the legal and financial expenditures that create permanent rigidities in public spending.

3.5 The program would attain these objectives through a multiplicity of sub-components. The following sections review the specific objectives of these and their outcomes. At the end of the chapter there are two rating sections: the first rates the entire FIAL series as a whole and the second each of the FIAL loans. The macroeconomic framework and the overall fiscal commitment of the FIAL series are rated in chapter 4 Section E.

B. Revenue Rigidities and Tax Reform

3.6 On the tax side, the objectives of the program were: (a) increasing collection; and (b) doing so while eliminating the main rigidities that introduced inefficiencies in taxation, which included prominently innumerable exemptions to income tax and Value Added Tax (VAT) as well as the multiple VAT rates applied to different activities. At the time of the FIAL design, the government had added a new distortion to the tax system: the tax on financial transactions, which is a classic example of a distorting tax (it is easy to evade by distorting behavior in an inefficient way, as people can avoid paying it by avoiding the use of the financial system, which reduces financial intermediation, which in turn reduces the overall efficiency of the economy).

3.7 The tax component of the FIAL aimed at reducing these rigidities and inefficiencies with three sub-components, which are briefly reviewed in the following subsections.

Rut (Registro Único Fiscal, Or Tax Registry)

3.8 The FIAL program supported the establishment of the RUT. The RUT would identify each taxpayer with a unique number, which then would become an instrument of tax compliance control because it would be used in all transactions carried out in the country. A number similar to the RUT already existed in Colombia; the program supported its substitution with the more flexible RUT, which had more digits and could convey more information. This condition was met. The PPAR rates the achievement of the objective of this sub-component substantial, and the outcome satisfactory.

New Laws and Regulations

3.9 This sub-component relied on the enactment of two laws (Laws 788 and 863), which were duly enacted, formally complying with the conditions in this respect. Yet, their enactment did not produce the expected results, in such a way that the formal compliance did not mean compliance in substance.

3.10 Law 788. The most important objective of the enactment of Tax Reform Law 788 in December 2002 was the elimination of exemptions and the expansion of the tax base for the Value Added Tax (VAT).⁴ Certainly, some of these exemptions were eliminated and the variety of VAT rates was reduced. Yet, four years later, the IMF Stand-By document for 2006 states the following:

3.11 “The authorities will submit legislation by August 2006 to reform the tax system, which is highly complex and distortionary with 9 VAT rates and the highest top income tax rate in the region at 38.5 percent (structural benchmark). Key elements of the authorities’ proposals would include reducing the number of VAT rates, and broadening the base; lowering the top income tax rate and curtailing exemptions and deductions, and

⁴ Other objectives included: (i) establishing a new ceiling on the wage exemption for personal income tax, and reducing incentives for non-taxed compensation to employees; and (ii) phasing out the corporate income tax exemption for capital gains from sales of stock, mutual funds and real estate and for profits from previously privileged corporate forms, contracts, funds or bonds.

possibly reducing the minimum threshold of income subject to tax; and diminishing the distorting effects of the financial transactions tax (FTT) by lowering the rate (currently 0.4 percent) or by making FTT payments deductible from the income tax. They are also considering a proposal to retain the tax on wealth (which was set to expire), with the revenues to be earmarked for additional military spending. The staff urged the authorities to also trim the so-called para-fiscal taxes (small payroll taxes earmarked to fund various social programs), which raise non-wage labor costs and deter formal sector employment. The authorities were sympathetic to this view but saw little political support for progress in this area.”

3.12 The problems mentioned in this paragraph are very similar to those that the FIALs had supposedly resolved.⁵

3.13 Law 863. On December 29, 2003, Congress passed Law 863, which made further improvements in tax policy, but also introduced new distortions to the tax system. Regarding this Law, the 2005 Country Economic Memorandum says the following:

3.14 “Although most of the reforms enacted in 2003 were desirable, two were not. Overriding Law 788 of 2002, which specified that the 10 percent surcharge under the corporate income tax would be reduced to 5 percent in 2005, Law 863 (Article 7) instead extended the 10 percent surcharge for 2005 and 2006. This policy change is undesirable since the base tax rate of 35 percent is already high by international standards. This discourages capital formation, including foreign direct investment, and encourages transfer pricing schemes and other manipulations by multinational firms thereby reducing Colombian tax revenues. A preferable approach would be to expand the corporate income tax base by eliminating more exemptions. Law 863 also raised the tax rate of the financial transactions tax from 0.3 percent to 0.4 percent of the transactions.”⁶

3.15 In sum, the government complied with the formal conditions by enacting the two laws mentioned in the sub-component. Yet, one of the laws left in place most of the distortions present in the tax legislation and the other actually worsened the deficiencies of the system by increasing the tax on financial transactions. That is, removing distortions was the ultimate objective of this component but instead they became worse. The PPAR rates the achievement of the objective of this sub-component negligible, and the outcome highly unsatisfactory.

Improving Tax Administration

3.16 The actions contained in the original policy matrix in this dimension were taken from the modernization plan of the National Tax and Customs Office at the Ministry of Finance (DIAN, its acronym in Spanish), which was supported through the Bank-funded Second Public Financial Management Technical Assistance Loan (PFMP II, or MAFP II in Spanish). These plans included the design and installation of a model of income

⁵ In spite of the intentions expressed by the IMF report, the government requested and obtained in 2006 an extension of the life of the financial transactions tax.

⁶ Colombia Country Economic Memorandum, The Foundations for Competitiveness, November 8, 2005, Report No. 32035-CO, pp. 133.

control called MUISCA in Spanish as well as many other activities aimed at improving DIAN's ability to track its customers. The plan was implemented successfully.

3.17 One of the measures that the tax authorities mentioned as most effective in improving the collection of the VAT and the income tax, however, raises an important issue of fiscal equity. Such measure is the devolution of 2 points of the VAT when the purchases that originate the tax are made with credit or debit cards. Having the payments made with such cards greatly increases the tax administration's ability to compare income tax and expenditures information to guide tax inspections. Yet, the measure discriminates against the people who do not have access to credit or debit cards, which tend to be the poor and the people living faraway from the banking system. In a country with 27 percent of the population living in rural areas, 18 percent living under \$2 per day, only 2 percent paying income tax, and a ratio of total deposits to GDP of 26 percent, the number of people paying 2 points of VAT more than the rest of the population just because they do not have access to credit or debit cards would seem to be substantial.⁷ This is a major distortion that was introduced with the 2003 reforms, which biases the VAT against the poor and those without banking services.

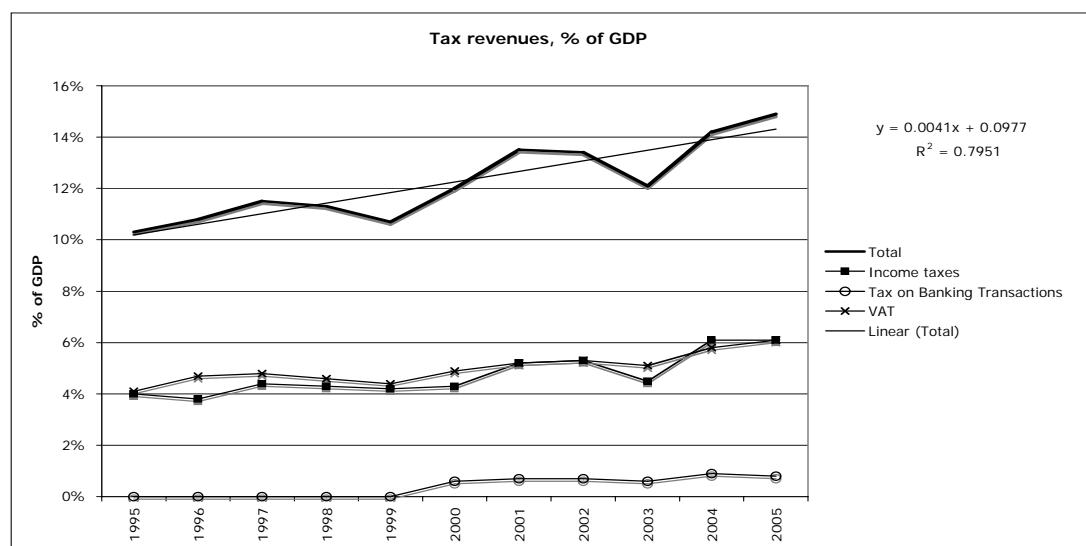
3.18 This report considers that the equity issue in the collection of taxes negatively affects the otherwise satisfactory structural improvement of tax administration. For this reason, this report rates the outcome of the Tax Administration sub-component moderately satisfactory, while it rates the achievement of objectives substantial.

Summary of Revenue Rigidities and Tax Reform

3.19 There are three aspects to taxation performance. First, there are the structural problems that the FIAL addressed, mainly related to the large number of tax rates and exemptions that characterize the Colombian system. These structural problems still exist and, according to the IMF and the Bank's Country Economic Memorandum, they are still substantial—they are, in fact, the main problems in today's tax legislation and administration. Some of these problems actually became worse as a result of laws enacted under the FIAL program. Second, there were substantial advances in tax administration, which were attained with the support of PFMP II.

3.20 The third aspect is revenue performance since the beginning of the FIALs. The central government made a serious effort to increase tax revenues since the early 1990s, with very good results: tax revenues rose from 10.3 to 14.9 percent of GDP in the last ten years (Figure 6).

⁷ There are only 1.4 million registered income tax payers in a country with 50 million inhabitants. Only 70 percent of the registered people make some payment. Sources of data: poverty and rural population from World Development Indicators (World Bank); ratio of deposits to GDP from International Financial Statistics (IMF); income tax payers from DIAN.

Figure 6. Tax Revenues, percent of GDP

Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

3.21 This improvement could be attributed to several factors—including improvements in the tax structure, in tax administration, and in overall economic performance.⁸ The ICR presents a decomposition of the growth of tax revenues into the effects of each of the four tax laws that were modified during the period, in such a way that nothing is left to allow for the improvement in tax administration. There is no way, however, to prove that this decomposition corresponds to reality. In the opinion of the IEG mission, based on several indicators provided by the DIAN, it seems that the increase in the tax collection as a percent of GDP is due mainly to improvements in tax administration. This cannot be proved, either. Thus, this component was evaluated based on the following facts:

- Tax collection increased very rapidly which, discarding an effect of tax buoyancy, may have been caused by improvements in tax administration, or in the structure of the taxes.
- Regarding these two possibilities, there was a very rapid improvement in tax administration and a highly unsatisfactory progress in the structural reform of the taxes themselves.

3.22 Based on these facts, and considering that one of the main objectives of the program was the reduction or elimination of tax rigidities, this report rates the outcome of the revenue rigidities sub-component unsatisfactory, and the achievement of the objective of this sub-component modest. The ICR rated this component satisfactory. IEG's ICR Review of FIAL III, the only review that rates the components of the FIALs, rates the

⁸ It is well known that there is buoyancy in tax systems, which results in increases in collection as a percent of GDP when GDP or income per capita increases. In the case of Colombia, for example, this can be seen in the behavior of income taxes paid by Ecopetrol, the profits of which increased from 2.3 to 3.6 percent of GDP from 2002 to 2005. At a maximum rate of 35 percent, the income taxes paid by this corporation would have increased from 0.8 to 1.2 percent of GDP, making for a difference of 0.4 percent of GDP.

achievement of the objective for tax administration high and in tax structural reforms modest, mostly for the same reasons cited in this report.

C. Public Administration

3.23 The backbone of the public sector reform process was the Programa de Renovación de la Administración Pública (PRAP), led by the National Planning Department (DNP), and based upon Presidential Directive 10 of October 2002. This program had so-called “vertical” reforms, which were basically sector or entity-specific institutional restructuring actions seeking to reduce excess public sector employment and enhance the quality and cost-effectiveness of public services; and “horizontal” reforms, which encompassed cross-sector issues of public administration, such as asset management, procurement, and others. During the second semester of 2002, the government agreed with the multilateral banks that the public sector reform process would be supported by structural adjustment loans from both the Bank and the Inter-American Development Bank (IDB). The Bank focused on the achievement of efficiency gains in the “horizontal” elements of the reform process.⁹ The IDB, on the other hand, focused its adjustment lending on the “vertical” elements of reform, and some horizontal elements not covered by the Bank. The following subsections summarize the sub-components of the Public Administration component.

Improving the Budget

3.24 The Colombian budgeting system was plagued by numerous structural problems at the time of the FIAL design. The program documents identified as the worst of these the rigidities created by earmarked revenues, which eliminated the fiscal space needed to accommodate revenue shocks or changes in expenditure priorities. Budgetary allocations actually authorized spending agencies to commit resources.¹⁰ This led to large accumulations of arrears in years when revenues fell below expected levels (which occurred quite often). In terms of the composition of expenditure, budget rigidity derived from high levels of both “structural” expenditures (such as pensions, debt service, and transfers) and law-based permanent earmarks basically left fiscal authorities with no room to maneuver. Since eliminating these rigidities was the main component of the loan, this was the main sub-component of the program.

3.25 To address this problem, the FIAL aimed at persuading Congress to enact: (a) a constitutional reform giving the Executive Branch the necessary powers to manage the

⁹ Program document for a proposed second programmatic fiscal and institutional adjustment loan to the Republic of Colombia, Report No. 27068-CO, October 23, 2003, paragraph 21.

¹⁰ The FIAL documents identified other problems in this sub-component. They included: (i) a budget structure that is incompatible with economic, functional, or performance analyses; (ii) a Ministry of Finance with limited authority to regulate public expenditure aggregates; (iii) complex institutional arrangements that in effect divide the budget process into separate current expenditure and investment processes; (iv) budgeting definitions that do not fall under internationally accepted standards; (v) a lack of instruments to develop a medium-term vision of fiscal policy; and (vi) a lack of substantial evaluation of public expenditure results, among others. See program document for a proposed second programmatic fiscal and institutional adjustment loan to the Republic of Colombia, Report No. 27068-CO, October 23, 2003, paragraphs 2-3.

budget within fiscal targets; and (b) amendments to the organic budget law, which would turn these powers effective.

3.26 Congress passed neither the constitutional reform nor the amendments to the organic budget law. The component then focused on a series of less ambitious actions, which resulted in some improvements in the budgeting methodology.¹¹ Yet, the main problems leading to budget inflexibility are still there. As noted by the third FIAL ICR, the lack of structural progress in the budget system was one of the reasons why the FIAL program did not progress into its fourth and final loan.¹²

3.27 Moreover, as discussed in a subsequent subsection, the program contained a sub-component that aimed at earmarking the royalty revenues received by the government, contradicting the overall objective of eliminating the rigidities affecting the budget. This report rates the outcome of this component highly unsatisfactory, noting that it was fundamental to the success of the program.

Fiscal Responsibility

3.28 The key expected results of this sub-component were: (i) enactment of measures by the Government for signaling and disclosing fiscal targets; and (ii) collection and publication of reliable fiscal sustainability data by the Central Government for the 50 largest sub-national governments. The Government enacted Law 819 in 2003. Among the key principles of this new law were the establishment of a medium-term fiscal framework, guidelines for ensuring debt sustainability, definition of macroeconomic targets, and transparency measures such as the publication of tax expenditures and improved fiscal reports to Congress.

3.29 This report rates the outcome of this component satisfactory and the achievement of objectives substantial.

Public Sector Assets Management

3.30 The government was unable to track or even identify the totality of its assets at the time of the design of the FIAL program. The reforms carried out under the FIAL program were aimed at resolving this problem. The sub-component included the following activities:

- **Institutional setting.** The Technical Secretariat became responsible for the enactment of policies, under the supervision of a multi-sector commission created for the purpose. This setting is in place since 2004.
- **Legislation.** The government introduced flexibility in the procedures needed to dispose of the assets. This reform is still in process, with some pieces of legislation still missing.

¹¹ Congress enacted an organic statute of the budget, but this only puts together already existing regulations.

¹²Source: ICR on a loan in the amount of US\$100 million to the Republic of Colombia for a Programmatic Fiscal and Institutional Structural Adjustment Loan III, Report No. 34792-CO, page 15.

- **Information systems.** The system is already in place and the government is testing it with 145 of the 287 institutions of the central government.
- **Asset management.** The central government wants to sell or transfer most of the assets to the territorial entities. Up to mid-2006, it had sold assets for \$103 million, receiving 85 percent of this amount in cash. The government estimates that the remaining assets have a value of \$2 billion, of which \$700 million can be sold. The plan is to sell these in a massive sale with the help of an investment bank.

3.31 This report rates the outcome of this component satisfactory and the achievement of objectives modest.

Public Sector Procurement

3.32 The Law 80 of 1993 established the main principles under which public sector procurement works in Colombia. It opened the possibility of contracting out to the private sector the provision of public services. The government had prepared a series of legal reforms that would upgrade the system to international standards. These reforms were not approved by Congress.

3.33 The FIAL then supported improvements in the following aspects:

- **Policy coordination.** The government created an Inter-Sector Procurement Commission, with no staff, for this purpose. It has been working since 2004.
- **Simplification of procedures.** The government modified Law 80 to streamline the system and outsourced to the Chambers of Commerce the registry of participants.
- **Information.** The information about procurement is now available in the Internet. The government is developing a system to make procurement transactions in the Internet.

3.34 This report confirms the ICR rating of unsatisfactory and the achievement of objectives negligible.

Management by Results (Creation of an Evaluation Office)

3.35 This component was aimed at creating mechanisms to monitor and evaluate the government's activities and programs, which is part of a system of management by results. The unit in charge of these activities was created in the Planning Office. It has a very small staff which designs and subcontracts the evaluations. Up to mid-2006, 19 sectors and 170 institutions had participated in three main kinds of activities:

- **Focalized evaluations.** The Evaluation Unit has undertaken evaluation of social policies as well as assessments of proposals to change laws for the public administration.
- **Follow up of the National Plan.**
- **Evaluation of the activities of the Territorial governments.**

3.36 This report rates the outcome of this activity satisfactory and the achievement of objectives substantial.

Defense of the State

3.37 The public sector neglected for many years its judicial processes, to the extent that suing the state became a low-risk, profitable activity.

3.38 The FIALs supported the following activities.

- **Inventory.** The Government was able to determine the number and nature of the legal suits raised against it as well as the amounts of money at risk.
- **Realistic estimation of the contingent liabilities.** The Government created a statistical program with data provided from government lawyers which allows for a reasonable estimate of these liabilities.
- **Coordination.** The system coordinates the management of all cases involving amounts larger than 200,000 minimum salaries (the level of the minimum salaries is used as an index to compensate for inflation in Colombia). By mid-2006, the system was coordinating the management of 99,000 cases.

3.39 The report rates the outcome of this activity satisfactory and the achievement of objectives modest.

Management Contracts

3.40 The first experience with this component in FIAL I was badly designed and was a failure. The program began with two institutions that are under the Ministry of Social Protection, ICBF (Instituto Colombiano de Bienestar Familiar, Colombian Institute for Family Welfare), which deals with family issues, and SENA (Servicio Nacional de Aprendizaje, National Training Service) which deals with workers' training. The management contract with these institutions included some technical goals and, mainly, goals in terms of collections of the payroll taxes that workers must contribute to these institutions. According to the contract, the government would provide a subsidy if the institutions collected a certain amount. In actuality, even if the institutions failed to collect the specified amounts, the government would still provide the subsidy because, legally, it had to. That is, the contract and the incentives contained in it were irrelevant. After this experience, the government wanted to eliminate this component in the subsequent FIALs but the Bank insisted that it was essential to have it. The component was retained and the subsequent experiences were quite negative because, as the government insisted, the mechanism does not work when the government has to provide the so-called incentives—budgetary allocations—even when the contracting institutions did not comply with their promises.

3.41 This report rates the outcome of this activity unsatisfactory and the achievement of objectives negligible.

Development of Incentives for Efficiency Gains (Earmarking Royalties)

3.42 Notwithstanding its name, this component in actuality created a new dimension of budget rigidity: earmarking to certain activities the royalties received by the government. Doing that required obtaining popular approval in the 2003 Referendum, which contained a question proposing their explicit distribution for education (56 percent), sanitation (36 percent), a sub-national pension fund (7 percent), and the conservation of the Cauca

River (1 percent). The failure of the Referendum prevented this rule to be hard-wired into the Constitution.

3.43 According to the arguments presented in the Bank's FIAL program documents, this measure was meant to counteract what was widely perceived as corrupt and inefficient use of royalties, often in poorly planned or otherwise inappropriate investment projects. Existing laws (especially Law 715) had established standards for efficiency and accountability for decentralized services; by ear-marking funds for these services, the expectation was improving the value-for-money.

3.44 However, earmarking resources clearly contradicts the declared objectives of the program, which is eliminating rigidities. Moreover, it is not clear that earmarked resources would be better managed or would lead to lower corruption than non-earmarked resources.

3.45 In fact, revenue earmarking is undesirable for several reasons.

- First, it generates a system of entitlements, which eliminates the incentives for efficiency because the beneficiaries of the entitlement know that they will receive their funds independently of their performance.
- Second, the system of entitlements establishes incentives to never achieve the expected results because, once these are achieved, the entitlements would disappear.
- Third, it introduces rigidity, which in turn is bad for two reasons:
- It makes it very difficult to shift budgetary allocations to meet changed priorities, and,
- It makes it very difficult to adjust the overall magnitudes of the budget to accommodate macroeconomic developments. This problem becomes a very difficult problem when there are fiscal or economic setbacks that require immediate fiscal adjustments, such as those that prevailed when the fiscal operations started in Colombia.

3.46 In other words, in addition to introducing rigidities, earmarking resources tends to lower, rather than increase, accountability and efficiency since such resources flow regardless of the efficiency of their spending. Finally, in any case, reducing earmarking was one of the main objectives of the operation.

3.47 This report rates the outcome of this sub-component highly unsatisfactory, not because the government lost the referendum, but because it was, from the beginning, at odds with the objectives of the loan. The report rates the achievement of objectives negligible.

Summary of Public Administration

3.48 In summary, the Public Administration component had 8 sub-components, of which the outcomes of 4 were satisfactory, 2 were unsatisfactory, and 2 were highly unsatisfactory. The highly unsatisfactory ratings are given to those components that were especially important for the attainment of the program's main objectives of reduction of budget rigidity and overall improvement of efficiency. Averaging these ratings, this

report rates the outcome of the Public Administration component moderately unsatisfactory.

Summary of Components

3.49 Based on the previous analysis, Table 4 summarizes this PPAR's ratings for all the components of the FIAL program and compares them with the ratings provided by the ICR's and IEG's ICR reviews. The last column summarizes the reasons for the disagreement between this PPAR's ratings and those of the other documents. The rating of the Overall Fiscal Commitment is based on the analysis of Chapter 4, Section E.

Table 4. Summary of Ratings for the Components of the FIAL Program

COMPONENTS	ICR (OUTCOME)	IEG'S ICR REVIEW (ACHIEVEMENT OF OBJECTIVES)	PPAR (ACHIEVEMENT OF OBJECTIVES)	PPAR (OUTCOME)	REASONS FOR DISAGREEMENT
Overall fiscal commitment	Satisfactory	Substantial	Modest	Unsatisfactory	The fiscal situation improved but mostly because of the improvement in oil prices. The structural situation remains similar to that which prevailed during the crisis.
Revenue rigidities	Satisfactory	Not rated	Modest	Moderately Unsatisfactory	See below for sub-components
Tax Registry	Satisfactory	Not rated	Substantial	Satisfactory	
New laws / Regulations	Satisfactory	Modest	Negligible	Highly Unsatisfactory	Rather than diminishing, the distortions of the system worsened.
Tax admin.	Highly satisfactory	High	Substantial	Moderately satisfactory	Supported specifically by a technical assistance loan
Public Administration	Satisfactory		Modest	Moderately Unsatisfactory	The main components, specially the budget improvement and earmarking royalties, were highly unsatisfactory.
Improving the Budget	Unsatisfactory	Negligible impact	Negligible	Highly Unsatisfactory	There was no progress in this component, which was key for the operation.
Fiscal Responsibility	Satisfactory	Substantial	Substantial	Satisfactory	
Asset Management	Satisfactory	Modest	Modest	Satisfactory	
Procurement	Unsatisfactory	Negligible	Negligible	Unsatisfactory	
Evaluation Office	Not rated	Not rated	Substantial	Satisfactory	
Defense of the State	Satisfactory	Modest	Modest	Satisfactory	
Management Contracts	Moderately satisfactory	Not rated	Negligible	Unsatisfactory	Failed from the first FIAL. The system does not work when the government cannot credibly refuse to finance the contracting agency.
Earmarking Royalties	Moderately satisfactory	Substantial	Negligible	Highly unsatisfactory	The component aimed at increasing the fiscal rigidities.

Source: World Bank

D. Overall FIAL Rating

3.50 This section rates the entire series of FIAL loans, and compares the ratings with those contained in the ICRs and IEG's FIAL III Review (which in fact rated the entire FIAL series). The ICRs rated the individual loans, but they gave the same ratings to all the operations, as we are doing in this report.

3.51 **Quality at entry.** The quality at entry was unsatisfactory for several reasons.

- First, the program was overly complex and disjointed in its institutional implementation, to the point that it obscured the ultimate objectives of the loans, taxed the government's implementation capacity and discouraged the completion of the series of loans.
- Second, within this complexity, many of the components aimed at attaining objectives that had little impact on the attainment of the ultimate objective of improving fiscal performance in a sustainable way. This was the case, for example, of all the efforts invested in improving budget planning instruments, creating management contracts, creating an evaluation office and streamlining procurement procedures. All these activities were commendable. Yet, the borrower could meet all of them and still—as it happened—fail to improve the fiscal performance of the country in a sustainable way.
- Third, the program contained a glaring contradiction: it supported the earmarking of royalties while justifying the entire loan on the argument that earmarking and other rigidities should be eliminated.

3.52 **Relevance.** The objectives of the operations were consistent with the needs of the country and with the CAS. However, as noted in the previous paragraph, many of the objectives of the individual loan components did not have a determining effect on the attainment of the ultimate objective of the loan and, in one case (the earmarking of royalties), the activity was in direct contradiction to such objectives. IEG's Review of FIAL III rated relevance as modest, noting that the operation did not address the most important sources of budgetary rigidity, the earmarked expenditures. This PPAR agrees with the IEG's ICR Review comment: "as the FIAL Program advanced, its relevance progressively declined."

3.53 **Outcomes.** There is no doubt that the Colombian government obtained some satisfactory results in several of the sub-components included in the FIAL program. Yet, it obtained unsatisfactory results in a few fundamental sub-components, which outweigh in importance the positive outcomes of the other activities. This was true in the tax structure component—the main problems that the loans were supposed to resolve are still there—and in the institutional component—the budgetary rigidities are still there and the loan worsened them. Regarding the institutional impact, this was substantial in several public sector components—fiscal responsibility, public sector assets management, the creation of an evaluation office, and the defense of the state. The institutional development of the other four public sector activities—budgetary flexibility, management contracts, earmarking of royalties, and procurement—was negligible. Tax administration experienced a substantial institutional development although this was mostly a result of the accompanying technical assistance loan (PFMP II).

3.54 Balancing these facts, as well as those stated in the next chapter regarding the main fiscal indicators, this report rates the FIAL series moderately unsatisfactory. This confirms the rating of IEG's ICR Review of FIAL III. That report based such rating on the moderate relevance of the loan (it did not address the need to remove the country's fiscal rigidities), and the fact that the trigger for the envisioned FIAL IV was not achieved.

3.55 **Risks to development outcome.** The probability that the moderately unsatisfactory outcome of the FIALs will improve in the future is very low. There are two dimensions to the FIALs' risks to development outcome.

- First, while the combined public sector deficit went down since the beginning of the operations, it did so mainly because of an improvement in commodity prices that could be reversed anytime. As a result, the country is at least as fiscally vulnerable to a reversal in its terms of trade as it was when the operations were designed, aiming at reducing such vulnerability.
- Second, the government did not and still does not own the fundamental objective of the program: the elimination of budgetary rigidities.

3.56 The government's lack of ownership of the objective of eliminating earmarking can be seen in the IMF Review of the Stand-By arrangements with the Republic of Colombia, issued in June 2006. The report summarizes the 2006 strategy of the authorities regarding earmarking with the following words:

3.57 "Their strategy is to concentrate first on reforms of the tax code and intergovernmental transfers. They will continue with reforms of the public enterprise sector and revenue earmarking, but see no need for another round of pension reform at this stage...

3.58 The authorities are committed to implementing the budget decree issued in December 2005, which includes provisions to evaluate earmarked revenues in the 2007 budget. Based on this evaluation, the government would develop legislation to phase out revenue earmarking that has achieved its objective and to limit the introduction of new earmarking to a well-specified time period."¹³

3.59 That is, after the FIALs presented as their main objective the reduction of budgetary rigidities, which prominently included earmarking, the government has not yet decided on its policy about earmarking, is not ruling out the possibility of issuing new earmarked expenditures, and is considering the possibility of eliminating only those that have achieved their objectives. This undermines the credibility of the most important objective of the FIALs, and shows that the government's commitment to this objective is still lacking almost 4 years after the program was approved.

¹³ Colombia: Second Review Under the Stand-By Arrangement and Request for Rephasing of Purchases—Staff Report. IMF country report No. 06/234.

3.60 Overall, the institutional development aimed at reducing the fiscal rigidities of Colombia was negligible. Since the long-term outcomes of the FIAL depend crucially from institutional factors, this report rates the risk of development outcome as high.

3.61 **Bank performance.** The FIAL III IEG's ICR Review, which dealt with the entire FIAL series, rated the Bank's performance unsatisfactory, justifying that rating with the following words: "Quality at Entry was unsatisfactory, with the project design inadequate to achieve the stated objectives. Although the objective was to promote reforms addressing fiscal rigidities necessary to attain substantial fiscal adjustment, the most important sources of those rigidities were not addressed. And around half the project components were intended to produce outputs, rather than the outcomes that would reasonably be expected of the last operation in a programmatic series. In fact, in the absence of much of the legal framework envisioned at the start of the FIAL Program, it is questionable whether the Bank should have continued with the program and undertaken FIAL III." This report adds that, in addition to the reasons provided by the IEG's ICR Review, the quality at entry was unsatisfactory because it contained a component, earmarking royalties, which was in direct contradiction to the objectives of the loan. However, it rates the Bank performance moderately unsatisfactory to reflect the fact that several other components, while less connected to the ultimate objectives of the loan than those referred to by the IEG report, were satisfactorily accomplished.

3.62 **Borrower performance.** The government staff in charge of implementation worked seriously on the program and met most of the conditions of the loans. In this sense, the borrower's performance was satisfactory. Yet, the main structural objectives of the program were not attained and, as discussed in the next chapter, while tax revenues increased fast as a percent of GDP, expenditures increased even faster, voiding the purpose of the operations. Moreover, as noted by the IEG's ICR Review of FIAL III, "During the period of the FIAL Program, the balance of the Central Administration averaged -5.4 percent of GDP, which was partially offset by favorable cyclical developments. A structural deficit of this magnitude was inimical with the objective of the FIAL Program." For these reasons, the FIAL III IEG's ICR Review rated the operation unsatisfactory. This report upgrades this rating to moderately unsatisfactory to take into account the satisfactory completion of other objectives which, although less connected to the ultimate objectives of the operations than those referred to by the IEG's report, were satisfactorily accomplished.

E. FIAL Rating by Loan

3.63 As discussed in the Introduction, it is difficult to split the evaluation of the FIAL series into independent evaluations of each loan because: (a) the program was conceived and largely implemented as an integral operation; (b) the components were the same in all loans, and (c) the reasoning underlying the ratings for the entire program is valid for each of the loans as well. Low quality at entry and negligible institutional impact affected all the loans equally because they were imbedded in the project design. As shown in the next chapter, the third problem—the failure in attaining the ultimate objective of improving fiscal performance in a sustainable way—cannot be attributed to any particular sub-period within the execution of the FIAL series. Such performance failed to improve throughout the life of the program and for the same reasons.

3.64 The same can be said about the Bank's and the Borrower's performance. For these reasons, this report rates the FIAL as shown in Table 5.

Table 5. FIAL Rating by Loan

	Outcome	Institutional Development	Sustainability	Risk to Development Outcome	Bank Performance	Borrower Performance
PPAR						
FIAL I	Moderately Unsatisfactory			High	Moderately Unsatisfactory	Moderately Unsatisfactory
FIAL II	Moderately Unsatisfactory			High	Moderately Unsatisfactory	Moderately Unsatisfactory
FIAL III	Moderately Unsatisfactory			High	Moderately Unsatisfactory	Moderately Unsatisfactory
FIAL Series	Moderately Unsatisfactory			High	Moderately Unsatisfactory	Moderately Unsatisfactory
ICR						
FIAL I	Satisfactory	Substantial	Likely		Satisfactory	Satisfactory
FIAL II	Satisfactory	Modest	Likely		Satisfactory	Satisfactory
FIAL III	Satisfactory	Substantial	Likely		Satisfactory	Satisfactory
IEG's ICR Review						
FIAL I	Moderately Satisfactory	Likely	Modest		Satisfactory	Satisfactory
FIAL II	Moderately Satisfactory	Modest	Likely		Satisfactory	Satisfactory
FIAL III and the series	Moderately Unsatisfactory	Modest	Likely		Unsatisfactory	Unsatisfactory

Source: World Bank

4. The Combined Outcomes of the Fiscal Operations and their Risk to Development Outcomes

4.1 While the SFAL and the FIAL programs were different operations, actually they were parts of one single effort to improve the borrower's fiscal situation. The question that emerges after reviewing all the actions taken under both of them is whether they, taken as a whole, succeeded in improving the overall fiscal situation of Colombia in the main areas of concern at the time of approval of the loans.

4.2 The elimination or the substantial reduction of the fiscal rigidities, together with the improvement in the efficiency and accountability in public expenditure, were expected to produce concrete outcomes. These included the following.

- The fiscal benefits were expected to reach 2 points of GDP by 2006.
- The primary surplus was expected to be 4 percent of GDP.
- The NFPS deficit of 4 percent of GDP would be virtually eliminated by 2006.
- The ratio of net public sector debt to GDP would remain at slightly above 50 percent by 2006.

4.3 This chapter discusses these points in more detail. It is relevant not just for the evaluation of the overall objectives of the series of loans, but also for the evaluation of several loan components, including the outcomes of public debt management in the SFAL as well as the overall fiscal commitment in the FIAL loans and the macroeconomic framework in both the SFAL and the FIAL loans. It is also fundamental for the assessment of the risk to development outcomes of both operations.

4.4 In the discussion of the fiscal outcomes and their risks, it is important to keep in mind that the government of Colombia distinguishes four aggregates of the fiscal accounts:

- **The central administration.** This entity comprises all the ministries. This is the measure that in most countries is called the central government.
- **The central government.** This entity includes the central administration plus the social security and the decentralized agencies.
- **The non-financial public sector.** This measure includes the central government plus public sector enterprises and the regional and local entities.
- **The combined public sector.** This includes the non-financial public sector plus the profits of the central bank, the profits of FOGAFIN (Financial System Guarantee Fund), and the net cost of the restructuring of the financial system (the net cost of the financial crisis).

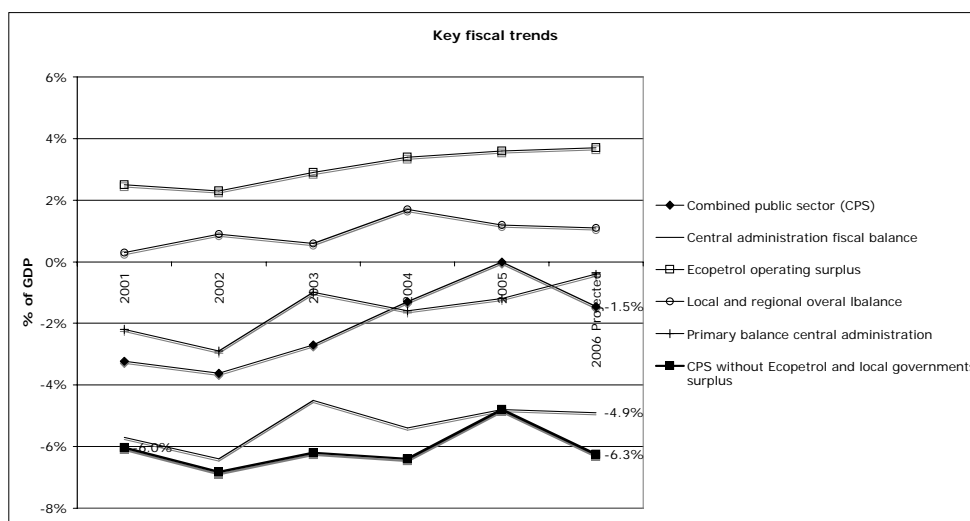
4.5 The following discussion centers on the most commonly-used aggregates: the central administration, the non-financial public sector, and the combined public sector.

A. Overall Risks

4.6 Figure 7 shows the trends of the main fiscal aggregates during the life of the fiscal operations. Notwithstanding improvements during 2001-2005, both extreme measures of the public sector in terms of their inclusiveness—the combined public sector and the central administration—were still in deficit at the end of 2005, as was the primary balance¹⁴ of the latter. For 2006, the government is projecting an improvement in the primary balance, which would decline from -1.2 percent in 2005 but would still be negative (-0.4 percent of GDP). The projections do not foresee a change in the overall balance, which stood at -4.9 percent of GDP.

4.7 The entity with the worst fiscal performance during the period of review was the central administration, which not only had very large overall deficits in the last few years but also primary deficits. The combined public sector was in a better condition largely because of: (a) the profits from Ecopetrol, the government-owned oil producer; and (b) the fiscal surpluses attained by the local and regional governments, which were due mainly to their limited implementation capacity.

Figure 7. Key Fiscal Trends



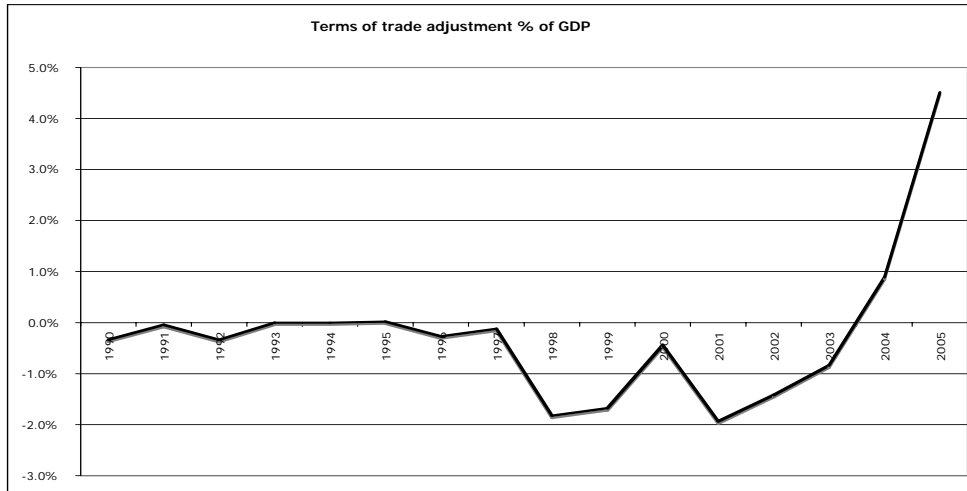
Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

4.8 The above picture is not encouraging for the country's fiscal sustainability. Without Ecopetrol, the non-financial public sector deficit would have been 5.2 percent of GDP in 2006, while the deficit of the combined public sector would have been 6.3 percent of GDP. These figures are worse than those prevailing in 2001 when the country was in a fiscal crisis (3.2 percent and 6.0 percent, respectively). Moreover, the primary balance of the central administration is still negative, meaning that the fundamental institution of the public sector is still borrowing to pay interest. And all this is happening

¹⁴ The primary balance is equal to the overall balance minus interest payments. Having this balance at zero or positive is a fundamental condition for stability.

while the economy is enjoying very favorable external circumstances. This can be seen in Figure 8, which shows the terms of trade adjustment that is used in the national accounts to convert exports in real terms into the country's real capacity to import. As can be seen in the figure, the Bank's fiscal operations started when this magnitude was at its lowest since 1990, and they ended when it was at its highest since that date. The turnaround was on the order of 6.5 percent of GDP.

Figure 8. Terms of trade adjustment % of GDP



Source: *World Development Indicators, World Bank.*

4.9 Thus, the fiscal situation is at least as risky as it was in 2001 in terms of the magnitude of the fiscal deficits, and the risk of a negative turn in the external conditions seems to be much higher than in that year because the deviation of the terms of trade relative to their average is much larger. Furthermore, it is almost certain that the profits of Ecopetrol are bound to decline as a percent of GDP. These profits have increased in the last few years by virtue of the oil price boom, which more than compensated for the simultaneous fall in the company's production in terms of barrels. The decline in production is irreversible if no new reserves are discovered. Thus, the profits of Ecopetrol can be maintained only in a world of continuously increasing oil prices. If these prices do not increase and in the absence of new reserves, this source of public sector funding is likely to disappear.

4.10 Concerns about the sustainability of the fiscal position of the combined and the non-financial public sectors are not limited to these points. As will be discussed in the following section, the government has been able to reduce these deficits only at the cost of reducing public sector investment.

B. The Risks of the Non-financial Public Sector Balances

4.11 As can be seen in Table 6, the overall fiscal balance of the widest measure of the public sector, the combined public sector, improved by 3.2 percent of GDP from 2001 to 2005. While increased tax collection accounted for a gain of 1.2 percent of GDP (37.1 percent of the total improvement), most of the fiscal gain was attained through a reduction of capital expenditure, which accounted for 2.3 percent of GDP (70.5 percent of the

improvement). As can also be seen in the table, the sustainability of the second most-inclusive measure of the fiscal operations, the non-financial public sector, also depends on keeping investment at its currently reduced levels. This contradicted one of the key conditions of the SFAL.

Table 6. Sources of Improvement in the Non-Financial Public Sector Fiscal Position 2001-2005

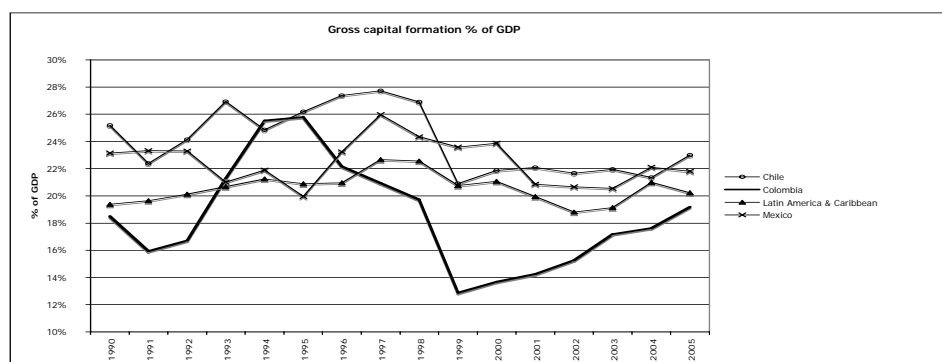
	Difference 2005-2001, % of GDP	% of overall improvement
Increased current expenditure	-0.5%	-14.4%
Statistical discrepancy	0.1%	2.9%
Reduced net lending	0.1%	2.9%
Increased non-tax revenue	0.3%	9.4%
Increased tax revenue	1.2%	37.1%
Reduced capital expenditure	2.3%	70.5%
Non-financial public sector balance	3.5%	107.8%
Central bank profits and other financial	-0.3%	-7.8%
Combined public sector balance	3.2%	100.0%

Note: Items that contributed to improving the fiscal situation have positive sign and vice versa.

Source: of Finance; Banco de la República; and Fund staff estimates.

4.12 The decline in public sector investment would not necessarily be a negative development if the private sector were investing in sectors previously managed by the government; if public sector investment had been unnecessary; or if, being less efficient than that carried out by the private sector, it had been crowding out the latter in the factor markets. Yet, there are two reasons to believe that none of these conditions is prevailing in Colombia. First, the government was obviously worried about this trend because reversing it was one of the objectives of the fiscal operations. Second, the decline in public sector investment has taken place in a country where, as shown in Figure 9, overall gross capital formation has been well below the levels of the Latin American region as a whole. This level has been increasing fast in the last few years, but it is still much lower than in two comparable countries, Chile and Mexico.

Figure 9. Gross Capital Formation % of GDP

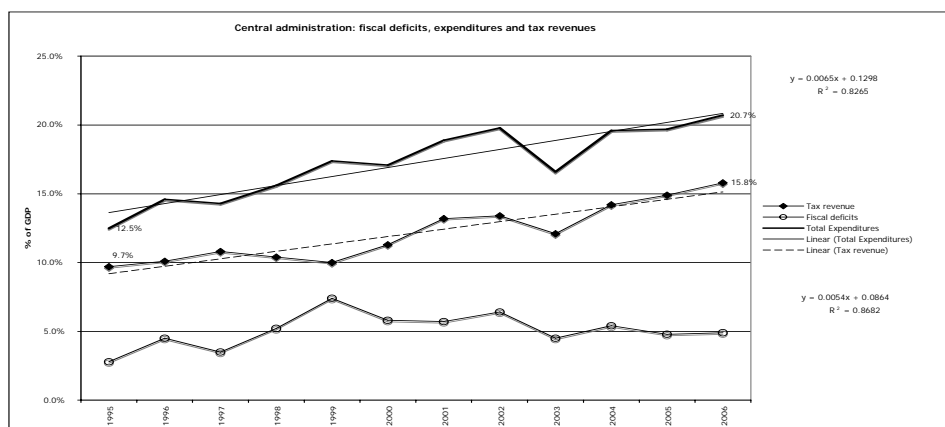


Source: World Development Indicators, World Bank.

C. Central Administration Risks: Taxes and Expenditures

4.13 Figure 10 shows that the improvement of the country's basic tax collection was not a recent phenomenon. It has been improving since 1995 and even before at approximately 0.54 percentage points of GDP per year. The problem is that total expenditures, which started from a larger basis, have been expanding at a higher rate (0.65 percentage points of GDP per year). As a result, the gap between total expenditures and tax revenues widened from 2.8 percent to 4.9 percent of GDP in ten years. If this trend continues, non-tax revenues would have to increase continuously as a percent of GDP to prevent the fiscal deficit from increasing. Or, in other words, the rate of growth of tax revenues is not enough to reduce or even maintain the central administration deficit.¹⁵ Hence, despite their satisfactory growth, tax collections have not been sufficient to support the rapid expansion of expenditures.

Figure 10. Central Administration: Comparative Trends

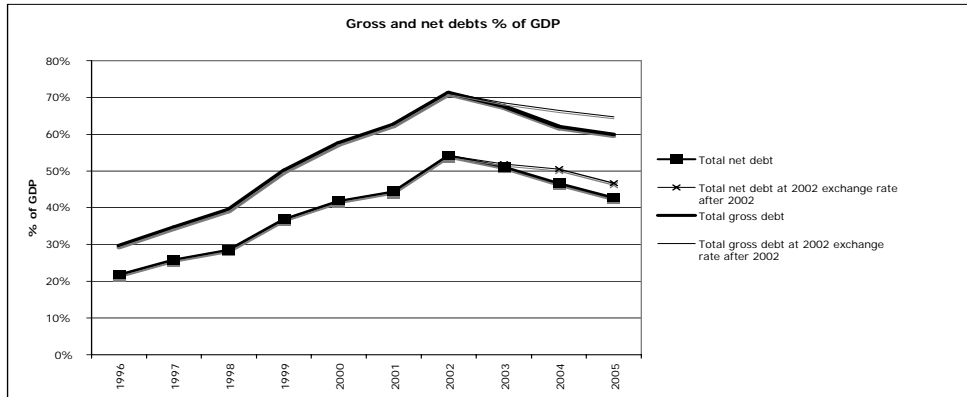


Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

D. The Risks of Debt and Interest Expenditures

4.14 The curves shown in Figure 11 provide an optimistic view of the debt situation for three reasons: (a) the net debt of the non-financial public sector (gross debt minus debt in any currency held by public sector institutions minus foreign currency held in the non-financial public sector) is much smaller than the gross one, mainly because many cash-generating institutions of the public sector accumulated assets during the period; (b) this net debt is low by international standards; and, (c) it fell by about 12 percentage points of GDP from 2002 to 2005.

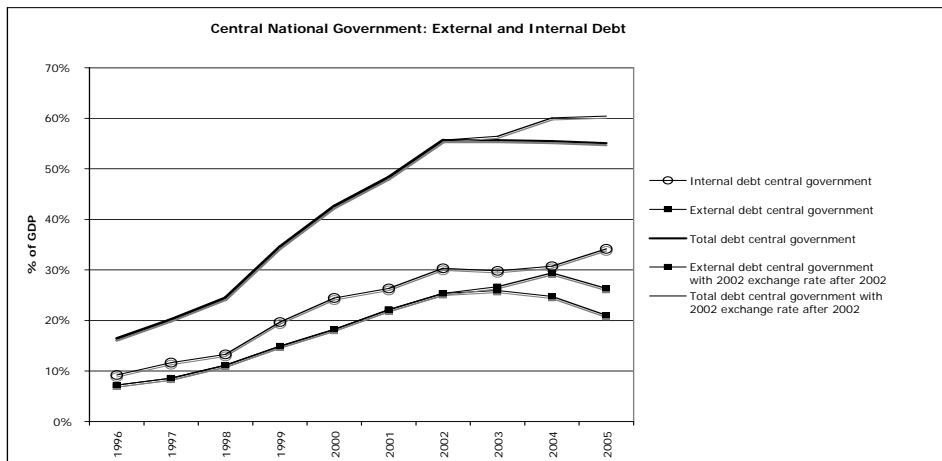
¹⁵ The central administration has been able to keep its deficit constant in spite of the trends shown in Figure 8 only because its non-tax revenues have increased substantially during the last few years.

Figure 11. Debt of the Non-Financial Public Sector, % of GDP

Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

4.15 There are two observations that should be made regarding this picture, however. First, the net debt concept may be deceptively optimistic in terms of reducing the burden of the debt of the public sector. For example, if the central government used the cash accumulated by other government institutions to service its own debt, or defaulted on the bonds it sold to them, the obligations of these other institutions would revert back to the central government, as is happening today with the pension liabilities. Or, if the central government used the resources of ECOPEPETROL to pay its debts, or defaulted on the debt it sold to Ecopetrol, it would diminish Ecopetrol's ability to invest, which in turn would revert in terms of larger deficits as a result of the company's declining oil production.

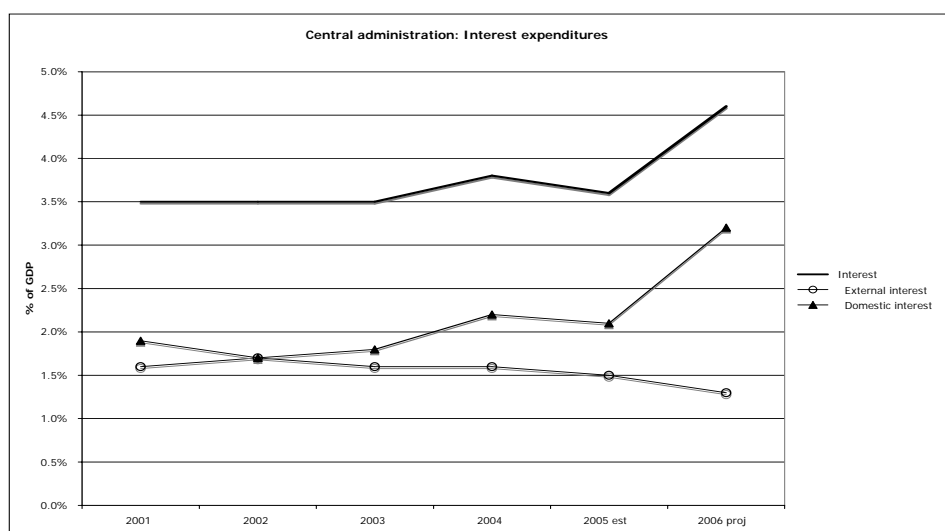
4.16 The second observation is that, as shown in Figure 12, rather than diminishing, the total debt of the central government remained constant as a percent of GDP since 2002. In fact, the total debt would have increased by 5 percent of GDP if the nominal exchange rate against the US Dollar had remained constant at its 2002 level. In other words, if the currency were to depreciate back to that level as a result of, say, a decline in commodity prices, the debt of the central government would be around 60 percent of GDP.

Figure 12. Central National Government: External And Internal Debt

Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

4.17 There was also sizeable substitution of domestic for external debt in 2005 (Figure 12), when the government prepaid \$3 billion in external debt while issuing a comparable amount in pesos in the domestic market. At the same time, there was an increase in the interest rates paid by the government. The increases in the interest rates on 10-year U.S. treasury bonds had triggered a depreciation of the peso of about 8 percent vis-à-vis the U.S. dollar starting in February 2006, together with a fall in equity prices and a rise in yields on government securities. The Government expects that these developments will result in an increase in interest payments equivalent to one percent of GDP in 2006 (Figure 13).

Figure 13. Central Administration Interest Payments



Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

E. Fiscal Commitment, Public Debt and Overall Risks

4.18 It is clear that the fiscal situation of Colombia improved markedly during the years of the fiscal operations. Yet, such improvements were mainly due to exogenous improvements in the Colombian economy. As is frequently the case, a country's economic variables become all positive when the prices of commodities are high and capital inflows substantial; conversely, the country's economy becomes depressed when those prices and inflows decline.

4.19 In the late 1990s and early 2000s, when the fiscal crisis was at its worst, everything conspired against the fiscal health of the country: the fall in commodity prices led to a fall in exports and GDP, and to a rapid depreciation of the currency; in turn, currency depreciation raised the debt burden; and the combined situation, aggravated by adverse political events, reduced capital inflows and turned them into net outflows. Since 2002, commodity prices have gone up and, with them, the country's exports and GDP; the currency appreciated, leading to a fall in the premium of peso over dollar interest rates and a decrease in the burden of the external debt; and dollar interest rates went

down to record low levels. That is, all the exogenous factors are favorable. Any deterioration in such circumstances would worsen the fiscal situation of the country again. The question is, has the country's fiscal vulnerability to a crisis declined as a result of the fiscal operations?

4.20 Given that the fiscal situation tends to deteriorate when there is an economic downturn, it is important to compare the 2005 situation with the one which prevailed just before the fiscal crisis. In 1997, the year before the 1998 crisis, the deficit of the core of the public sector, the central administration, was 3.5 percent of GDP. This deteriorated to 5.2 percent and 7.4 percent of GDP in 1998 and 1999, respectively. If the fiscal deficit deteriorated at the same pace today, it would reach 6.5 percent in one year and 8.7 percent in two years, creating a situation that would be much worse than that which the country faced at the turn of the century. The situation of the broadest measure of fiscal operations, the combined public sector, would deteriorate even faster if, as assumed, the country's terms of trade deteriorated as well, or if, as likely to happen regardless of the behavior of oil prices, Ecopetrol reduced its contributions to the government as a result of its investment needs.

4.21 It could be argued that the government would react more quickly this time to adjust expenditures to the lower level of revenues; yet, as it has been extensively discussed in the previous chapters, the budget remains very rigid, in some areas more so than in 1998.

4.22 We can conclude that:

- First, the central administration is not stronger than when the fiscal crisis started.
- Second, the burden of the debt is heavier. In 1997, the ratio of the central government debt to GDP was 20.2 percent of GDP; in 2005, it was 55.4 percent.

4.23 That is, the fiscal improvement of the central government is not likely to be sustained if there is a downturn in the economic activity of the country.

4.24 Given that the improvements in the non-financial public sector and the combined public sector largely depend on the prices of oil and on the limited implementation capacity of the local and regional governments—two factors that can change in the future—it seems that their fiscal balances are also prone to deteriorate very rapidly in case of a crisis.

4.25 For these reasons, and given that the objective of the FIAL program was to improve the fiscal situation in a structural way, independently of the circumstances, this report rates the Overall Fiscal Commitment of the FIAL program unsatisfactory. In terms of the achievement of the objectives, the report rates the program modest.

F. Summary and Overall Rating of the Combined Fiscal Operations

4.26 In summary:

- The balance of the non-financial public sector improved substantially, but mainly because of declining investment, increasing royalties resulting from atypically

- high oil prices, and expenditure delays resulting from the lack of implementation capacity at the regional levels.
- The primary balance of the central administration remained negative (-1.2 percent of GDP in 2005).
 - Regarding the public debt indicators, these improved as a result of a reduction in the ratio of external debt to GDP. Yet, such reduction was due to two major trends:
 - First, the currency appreciated in nominal and real terms. This, of course, is reversible.
 - Second, the government substituted domestic for external debt at the margin. This has increased the burden of the interest payments. The government estimates that this would represent an increase equivalent to one percent of GDP in 2006.
 - Also, as discussed in the previous chapters, the fiscal situation improved while the most important structural issues were not resolved.

4.27 For all these reasons, this report rates the improvements attained in the last few years as unsustainable in the face of a crisis. Therefore, the risk to development outcomes is rated as high for both operations.

4.28 These considerations apply not just to the operations as a whole but also to the macroeconomic framework and the over-all fiscal commitments of the SFAL and the FIAL series.

5. Lessons

5.1 The lessons learned in these operations are not new to the Bank.

- First, as noted in IEG’s ICR Review of FIAL III, project design needs to be clearly aligned with development objectives to attain the latter. Even if the structural deficit of the central administration is “highly sensitive and political” as the ICR states, the magnitudes of these structural rigidities were such that they must be addressed if progress is to be made in achieving the substantial fiscal adjustment that is required for sustained macroeconomic stability.
- Second, loans with large numbers of objectives and conditions, and involving too many institutions relative to the management capacity of the Government and the Bank itself, overtax the implementation capacity of both the Bank and the borrower and results in cumbersome execution. While there may be differences in opinion regarding what would be the maximum number of tasks that is practical to carry out under a loan, according to the opinions collected by the IEG mission in the country, practically all the people involved in the implementation of this operation thought that the number of objectives, conditions and participating institutions in these operations was excessive and felt that they overtaxed the Bank’s and the borrower’s implementation capacities and dispersed the energies of reform. Just the FIALs had 10 sub-components, with an average of four to five activities per sub-component that should be performed to meet the sub-component objectives. Given that there were 3 FIALs (there were originally 4 but one was dropped), this made for roughly 150 sub-activities, which required follow up, comments, discussions and recommendations.
- Third, the inclusion of objectives of widely different levels of priority and weak connection with the ultimate goals of the operations tends to obscure the degree of attainment of the latter. In the operations reviewed in this report, the impact on the fundamental goals of the operations of many of the sub-components, activities and sub-activities was very tenuous. This mix of highly important with much less important activities obscured the ultimate objectives of the operation to the point that the government could comply with most of the objectives of the components and sub-components and still fail to comply with the fundamental objectives of the loan.
- Fourth, success depends on the borrower’s ownership of the objectives of the loan. The reviewed operations met this condition at a very general level—the government wanted to improve its fiscal condition. Yet, the government did not actually share the objective of reducing the rigidity of the system. This was evident in several ways:
 - As noted in the IEG’s ICR Review of the FIAL III, these operations did not address the main rigidities—the ones related to the transfers to the local and regional governments—even if their President’s Report recognized their importance.
 - The SFAL supported a reform that actually increased the rigidity of the system.

- The FIAL program also included an important reform that would worsen the rigidity of the system, not just in terms of quantities but also in terms of their allocation: the plan to earmark the royalties received by the government.
- As noted in paragraph 3.59, “after the FIALs presented as their main objective the reduction of budgetary rigidities, which included earmarking prominently, the government has not yet decided its policy about earmarking, is not ruling out the possibility of issuing new earmarked expenditures and is considering the possibility of eliminating only those that have achieved their objectives. This undermines the credibility of the most important objective of the FIALs and shows that its commitment to this objective is still lacking almost 4 years after the Program was approved.”
- Also, there was another sub-component, the management contracts, which the Bank insisted in including in the FIALs against the opinion of the government. The lack of ownership was one of the reasons for the failure of this sub-component.

Statistical Annex

Table 7. Fiscal Balances

	2001	2002	2003	2004	2005	2006*
Total revenue	29.5%	29.5%	30.0%	30.3%	31.0%	31.2%
Current revenue	29.5%	29.5%	30.0%	30.3%	31.0%	31.2%
Tax revenue	19.2%	19.1%	19.5%	19.6%	20.4%	20.9%
Non-tax revenue	10.3%	10.4%	10.5%	10.7%	10.6%	10.2%
Financial income	1.3%	0.9%	1.1%	1.5%	1.5%	1.5%
Operating surplus of public enterprises	4.2%	4.0%	4.6%	3.4%	3.9%	3.8%
Of which: Ecopetrol	2.5%	2.3%	2.9%	3.4%	3.6%	3.7%
Other	4.8%	5.4%	4.8%	5.7%	5.2%	4.9%
Total expenditure and net lending 1/	33.2%	33.5%	32.5%	31.5%	31.3%	32.7%
Current expenditure	24.9%	25.9%	24.3%	25.9%	25.4%	26.3%
Wages and salaries	7.5%	8.0%	7.3%	7.0%	7.1%	7.0%
Goods and services	3.5%	3.4%	3.3%	4.4%	4.6%	4.4%
Interest	5.0%	4.5%	4.7%	4.8%	4.0%	4.8%
External	2.3%	2.1%	2.1%	1.9%	1.6%	1.5%
Domestic	2.8%	2.4%	2.7%	2.8%	2.4%	3.4%
Transfers to private sector	9.8%	9.8%	9.1%	7.8%	7.8%	7.9%
Of which: from social security	6.5%	6.7%	6.9%	6.9%	6.8%	6.9%
Other 2/	-0.9%	0.2%	-0.1%	1.9%	1.9%	2.1%
Capital expenditure	8.2%	7.6%	8.2%	5.7%	5.9%	6.4%
Fixed capital formation (cash basis)	8.2%	7.4%	8.1%	5.6%	5.9%	6.3%
Other (including floating debt) 3/	0.0%	0.0%	0.1%	0.0%	0.0%	0.0%
Transfers	0.1%	0.2%	0.1%	0.1%	0.0%	0.0%
Net lending	0.1%	0.1%	0.0%	0.0%	0.0%	0.0%
Statistical discrepancy	0.2%	-0.1%	-0.3%	-0.3%	0.3%	0.0%
Non-financial public sector balance	-3.5%	-4.2%	-3.2%	-1.5%	0.0%	-1.5%
Quasi-fiscal balance (BR cash profits)	0.7%	0.8%	0.6%	0.5%	0.2%	0.3%
Fogafin balance	0.2%	0.3%	0.3%	0.3%	0.2%	0.1%
Net cost of financial restructuring 4/	-0.7%	-0.6%	-0.4%	-0.5%	-0.4%	-0.4%

^{1/} The information on local governments has been significantly revised starting in 2004, leading to large changes in reported public investment and other non-tax revenues and other current spending.

^{2/} Expenditure reported on commitments basis.

^{3/} Includes adjustments to put spending on commitment basis and the change in unpaid bills of selected non-financial public enterprises.

^{4/} Interest payments on public banks restructuring bonds and mortgage debt relief related costs.

* Projected

Source: Ministry of Finance; Banco de la República; and Fund staff estimates.

Table 8. Operations of the Central Government

Includes Central Administration, Social Security And Decentralized Agencies							
	2000	2001	2002	2003	2004	2005 est	2006 p
Total revenue	18.7%	20.3%	19.7%	20.8%	22.0%	22.0%	23.2%
Current revenue	18.5%	20.3%	19.7%	20.7%	21.6%	21.7%	23.2%
Tax revenue	14.6%	16.5%	16.4%	16.9%	17.7%	17.4%	18.5%
Non-tax revenue	3.2%	3.0%	2.6%	3.2%	3.4%	3.2%	3.3%
Property income	0.8%	1.1%	0.7%	0.9%	0.9%	1.2%	1.2%
Other	2.4%	1.9%	1.8%	2.3%	2.6%	1.9%	2.1%
Current transfer receipts	0.7%	0.8%	0.8%	0.6%	0.5%	1.2%	1.4%
Local government	0.0%	0.0%	0.0%	0.0%	0.0%	0.7%	0.7%
Local enterprises	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Local non-financial public sector	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
National enterprises	0.7%	0.7%	0.8%	0.6%	0.5%	0.5%	0.7%
Private sector	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Capital revenue	0.2%	0.0%	0.0%	0.1%	0.4%	0.3%	0.0%
Total expenditure and net lending	23.0%	25.1%	25.3%	24.5%	25.7%	24.6%	26.3%
Current expenditure	19.1%	20.4%	22.0%	20.6%	21.8%	20.8%	22.3%
Wages and salaries	3.4%	3.5%	3.4%	3.2%	3.0%	2.7%	2.9%
Goods and services	2.2%	2.4%	2.2%	2.3%	2.3%	2.1%	2.4%
Interest	3.0%	3.7%	3.5%	3.9%	3.8%	3.5%	4.2%
External	1.2%	1.7%	1.7%	1.8%	1.6%	1.5%	1.3%
Domestic	1.8%	1.9%	1.7%	2.1%	2.2%	2.0%	2.9%
Transfers to	10.6%	11.7%	12.3%	11.7%	12.2%	12.4%	12.8%
Local governments	3.0%	3.4%	4.0%	3.5%	3.4%	3.3%	3.3%
Local enterprises	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Local non-financial public sector	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
National enterprises	0.0%	0.0%	0.2%	0.1%	0.1%	0.0%	0.0%
Private sector	7.7%	8.3%	8.0%	8.1%	8.8%	9.1%	9.5%
Other currency expenditure	-0.1%	-0.9%	0.6%	-0.5%	0.5%	0.0%	0.0%
Capital expenditure	3.4%	4.2%	3.0%	3.5%	3.8%	3.9%	4.2%
Fixed Capital Formation	1.6%	2.1%	1.9%	1.8%	2.1%	2.4%	2.7%
Transfers to	1.8%	2.2%	1.1%	1.8%	1.7%	1.6%	1.5%
Local governments	1.7%	1.9%	1.0%	1.6%	1.5%	1.5%	1.5%
Local enterprises	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Local non-financial public sector	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
National enterprises	0.1%	0.2%	0.0%	0.1%	0.1%	0.0%	0.0%
Private sector	0.1%	0.1%	0.0%	0.1%	0.1%	0.0%	0.0%
Net lending	0.4%	0.5%	0.4%	0.4%	0.1%	-0.1%	-0.2%
Overall Balance	-4.3%	-4.8%	-5.6%	-3.7%	-3.7%	-2.6%	-3.1%

Table 9. Operations of the Central Administration

	2001	2002	2003	2004	2005 est	2006 proj
Total revenue	14.7%	15.0%	13.3%	15.5%	16.1%	17.4%
Current revenue	14.7%	15.0%	13.3%	15.5%	16.1%	17.4%
Tax revenue 1/	13.2%	13.4%	12.1%	14.2%	14.9%	15.8%
Net income tax and profits	5.3%	5.3%	4.5%	6.1%	6.1%	6.9%
Goods and services	5.9%	5.8%	5.5%	6.2%	6.5%	6.6%
VAT	5.3%	5.3%	5.1%	5.8%	6.1%	6.2%
Gasoline	0.6%	0.5%	0.4%	0.4%	0.4%	0.4%
International trade	1.1%	1.0%	0.8%	0.9%	1.0%	1.0%
Financial transactions tax	0.8%	0.7%	0.6%	0.9%	0.8%	0.8%
Stamp and other taxes	0.0%	0.7%	0.7%	0.2%	0.4%	0.5%
Non-tax revenue	1.5%	1.6%	1.2%	1.2%	1.2%	1.6%
Property	0.3%	0.3%	0.2%	0.2%	0.2%	0.2%
Other	1.2%	1.3%	1.0%	1.1%	1.1%	1.5%
Total expenditure and net lending	20.4%	21.4%	17.8%	20.9%	21.0%	22.4%
Current expenditure	15.8%	18.2%	14.7%	17.5%	17.9%	19.0%
Wages and salaries	3.0%	3.0%	2.6%	2.8%	2.5%	2.6%
Goods and services	1.5%	1.5%	1.3%	1.4%	1.5%	1.6%
Interest	3.5%	3.5%	3.5%	3.8%	3.6%	4.6%
External interest	1.6%	1.7%	1.6%	1.6%	1.5%	1.3%
Domestic interest	1.9%	1.7%	1.8%	2.2%	2.1%	3.2%
Other expenditure 2/	-0.9%	0.7%	-0.5%	0.5%	0.0%	0.0%
Current transfers 3/	8.6%	9.5%	7.8%	9.1%	10.2%	10.2%
Capital expenditure	3.8%	2.5%	2.7%	3.3%	3.0%	3.2%
Fixed capital formation 2/	1.3%	1.3%	1.0%	1.4%	1.1%	1.8%
Capital transfers	2.5%	1.2%	1.7%	1.9%	1.9%	1.5%
Net lending	0.8%	0.6%	0.3%	0.1%	0.1%	0.2%
Overall balance	-5.7%	-6.4%	-4.5%	-5.4%	-4.8%	-4.9%
Memorandum						
Primary balance	-2.2%	-2.9%	-1.0%	-1.6%	-1.2%	-0.4%

Annex A. Basic Data Sheet

STRUCTURAL FISCAL ADJUSTMENT PROJECT (TF-26673; FSLT-70920)

Key Project Data *(amounts in US\$ million)*

	Appraisal estimate	Actual or current estimate	Actual as % of appraisal estimate
Total project costs	400	400	100%
Loan amount	400	400	100%
Cofinancing			
Cancellation			
Institutional performance			

Project Dates

	Original	Actual
Initiating memorandum	07/16/2001	09/17/2001
Negotiations	11/07/2001	11/07/2001
Board approval	12/18/2001	12/18/2001
Signing	12/19/2001	12/19/2001
Effectiveness	12/20/2001	12/20/2001
Closing date		02/21/2003

Mission Data

	Date (month/year)	No. of persons	Staff days in field	Specializations represented	Performance rating	Rating trend	Types of problems
Identification/ Preparation	Feb to Mar 2001	12		TTL (2); Consultant (2); Program Asst. (1); Economists (Health, Pensions, Macro, Fiscal) (5); Decentralization (1)	S		
	Apr 2001	11		TTL (2); Consultant (2); Program Asst. (1); Economists (Health, Pensions, Macro, Fiscal) (5); Decentralization	S		

	<i>Date (month/year)</i>	<i>No. of persons</i>	<i>Staff days in field</i>	<i>Specializations represented</i>	<i>Performance rating</i>	<i>Rating trend</i>	<i>Types of problems</i>
				(1) meeting with counterparts / officials in Washington DC			
	May 2001	12		TTL (2); Consultant (2); Program Asst. (1); Economists (Health, Pensions, Macro, Fiscal) (5); Decentralization (1); Legal (1)	S		
	July 2001	12		TTL (2); Consultant (2); Program Asst. (1); Economists (Health, Pensions, Macro, Fiscal) (5); Decentralization (1); Legal (1)	S		
Appraisal	Nov 2001	12		TTL (2); Consultant (2); Program Asst. (1); Economists (Health, Pensions, Macro, Fiscal) (5); Decentralization (1); Legal (1) negotiations took lace in Bogota at the Bank's office	S		
Supervision	Jan 2002	2		TTL (2)	S		
	Feb 2002	2		TTL (2)	S		
	Aug 2002	7		TTL (2); Consultant (1); Health Sector/ISS (1); Social Security/ISS (1); Decentralization (1); Legal (1)	S		
Completion	Sep 2003	1		TTL (1)	S		

FIRST PROGRAMMATIC FISCAL AND INSTITUTIONAL ADJUSTMENT LOAN (LOAN 7167-CO)

Key Project Data *(amounts in US\$ million)*

	<i>Appraisal estimate</i>	<i>Actual or current estimate</i>	<i>Actual as % of appraisal estimate</i>
Total project costs	300	300	100%
Loan amount	300	300	100%
Cofinancing			
Cancellation			
Institutional performance			

Cumulative Estimated and Actual Disbursements

	<i>FY02</i>
Appraisal estimate (US\$M)	300
Actual (US\$M)	300
Actual as % of appraisal	100%
Date of final disbursement: March 20, 2003	

Project Dates

	<i>Original</i>	<i>Actual</i>
Initiating memorandum		11/22/2002
Negotiations	02/13/2003	02/13/2003
Board approval	07/08/2003	03/18/2003
Signing		03/19/2003
Effectiveness		03/20/2003
Closing date	---	04/30/2003

SECOND PROGRAMMATIC FISCAL AND INSTITUTIONAL STRUCTURAL ADJUSTMENT LOAN (LOAN 72010-CO)

Key Project Data *(amounts in US\$ million)*

	<i>Appraisal estimate</i>	<i>Actual or current estimate</i>	<i>Actual as % of appraisal estimate</i>
Total project costs	150	150	100%
Loan amount	150	150	100%
Cofinancing			
Cancellation			
Institutional performance			

Cumulative Estimated and Actual Disbursements

	<i>FY04</i>
Appraisal estimate (US\$M)	150
Actual (US\$M)	150
Actual as % of appraisal	100%
Date of final disbursement: November 24, 2003	

Project Dates

	<i>Original</i>	<i>Actual</i>
Initiating memorandum	07/28/2003	08/12/2003
Negotiations	10/21/2003	10/21/2003
Board approval	11/20/2003	11/20/2003
Signing	02/20/2004	11/24/2003
Effectiveness	11/24/2003	11/24/2003
Closing date	02/24/2004	02/24/2004

**<THIRD PROGRAMMATIC FISCAL AND INSTITUTIONAL STRUCTURAL
ADJUSTMENT LOAN (TF-53133; FSLT-72800)**

Key Project Data (*amounts in US\$ million*)

	<i>Appraisal estimate</i>	<i>Actual or current estimate</i>	<i>Actual as % of appraisal estimate</i>
Total project costs	100	100	100%
Loan amount	100	100	100%
Cofinancing			
Cancellation			
Institutional performance			

Cumulative Estimated and Actual Disbursements

	<i>FY95</i>
Appraisal estimate (US\$M)	100
Actual (US\$M)	100
Actual as % of appraisal	100%
Date of final disbursement: April 26, 2005	

Project Dates

	<i>Original</i>	<i>Actual</i>
Initiating memorandum	05/14/2004	10/05/2004
Negotiations	07/06/2004	11/09/2004
Board approval	08/19/2004	03/22/2005
Signing	---	04/04/2005
Effectiveness	04/26/2005	04/26/2005
Closing date	06/30/2005	06/30/2005

Staff Inputs (staff weeks)

	<i>No. of Staff Weeks</i>	<i>US\$ (000)</i>
Preappraisal	86.48	454.03
Appraisal		
Negotiations		
Supervision	18.46	63.67
Other		24.44
Total	104.94	542.15

Mission Data

	<i>Date (month/year)</i>	<i>No. of persons</i>	<i>Staff days in field</i>	<i>Specializations represented</i>	<i>Performance rating</i>	<i>Rating trend</i>	<i>Types of problems</i>
Identification/ Preparation	Oct 2004	52		Includes 25 consultants interventions and 27 staff interventions			
Appraisal	Nov 2004	3		Includes 1 consultant and 2 staff interventions			
	Feb 2005						
Supervision	Apr 2005			Includes 5 consultants interventions and 13 staff interventions			
Completion		3		Includes 3 consultants interventions			

Annex B. List of Persons Met

Ministry of Finance and the National Directorate of Taxes and Customs (DIAN):

Veronica Navas. Advisor of the Council of Fiscal Policy at the time of the FIALs

Claudia Rodriguez, Group of the Multilateral Institutions at the Ministry of Finance (the unit in charge of operations with multilaterals)

Alejandro Gamboa, Coordinator of the Group of Multilateral Institutions

Jose Luis Plaza, Hernando Gallo and Pastor Sierra, advisors of the DIAN

Department of National Planning (DNP):

Eliana Moreno, advisor, Program of Public Administration Reform

Julio Abril, Advisor, Evaluation of Public Policies

Jorge Vargas, Advisor of de Vice-Directorate of Credit at DNP, Management Contracts

Juan Pablo Toro, former Vice-Director of Credit at DNP (phone interview)

Roberto Aguado, Director, Project of Public Procurement

Eduardo Hernandez, Project of Asset Management

Marcela Montealegre, Budget Reforms

Fernando Jimenez, Budget Reforms

Banco de la Republica:

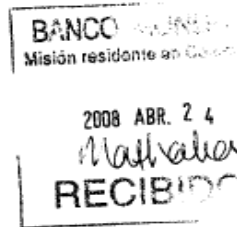
Jorge Toro, Vice-Manager, Economic Studies

Juan Mauricio Cortes, Director, Monetary Programming and Inflation

Gloria Alonso Masmela, Macroeconomic Programs

Annex C. Comments from Government

República de Colombia



Departamento Nacional
de Planeación DNP

SC - 20082300292621

Bogotá, D.C., martes 22 de abril de 2008

Señor
JAIME JARAMILLO VALLEJO
Acting Manager
Country Evaluation and Regional Relations Group
Independent Evaluation Group
Banco Mundial
Carrera 7 No. 71 - 21 torre A, piso 16
Ciudad

Asunto: Colombia: Structural Fiscal Adjustment Project (TF-26673; FSLT-70920); First Programmatic Fiscal and Institucional Adjustment Loan (Loan No 7163-CO); Second Programmatic Fiscal and Institucional Adjustment Loan (Loan No 72010-CO); Third First Programmatic Fiscal and Institucional Adjustment Loan (TF 53133; FSLT-72800) Draft Project Performance Assessment Report.

Apreciado señor Jaramillo:

Atendiendo a su comunicado del 11 de febrero de 2008, por medio del cual nos solicitaba revisar el borrador de reporte de evaluación realizado al programa de la referencia, me permito comunicarle que una vez revisado el documento, tenemos las siguientes observaciones que esperamos sean recogidas en la versión final del mismo:

1. Numeral 3.30 Public Sector Assets Management: En materia del Programa de Gestión de Activos, la Nación ha registrado varios avances, que se detallan en el documento adjunto.
2. Numeral 3.32 Public Sector Procurement: En la frase final del párrafo correspondiente, se presenta una inconsistencia ("These reforms were not approved by Congreso"). En efecto, debe aclararse que las reformas a que hace alusión la frase citada no fueron improbadas por el Congreso ya que no fueron puestas a su consideración debido al trámite legislativo. El Congreso, en consecuencia, no rechazó la iniciativa de reforma y la ausencia de trámite y discusión de los proyectos se debió a causas externas al Departamento Nacional de Planeación-DNP.

Es importante destacar que los objetivos perseguidos por el FIAL han sido alcanzados, y esto se evidencia a través de:

- i) Expedición de la Ley 1150 de 2007 por medio de la cual se modifica la Ley 80 de 1993 y el decreto 066 de 2008 sobre modalidades de selección, que la reglamenta. Este nuevo marco regulatorio ajustó los procedimientos de selección según el objeto de contratar, introdujo el

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procedimiento para la selección de consultores; modificó la selección de contratistas introduciendo el principio de "pasa no pasa", amplió el catálogo de garantías a utilizar en los contratos; modernizó la gestión de adquisición a través del uso de Internet y pretende generar ahorros y reducción en costos de transacción a través de métodos de selección que permitan explotar el poder de compra del Estado. Se considera que el esquema regulatorio Colombiano actual, en materia de contratación pública, cumple estándares internacionales.

- ii) La Comisión Intersectorial no sólo fue creada en el 2004 sino que desde esa fecha cuenta con un equipo de expertos que en calidad de Secretaría Técnica de al misma y desde el DNP coordinación y dirigen su labor, alcanzando metas como al aprobación de la Ley 1150 de 2008, la negociación de 4 TLCs y la coordinación tecnológica entre el Sistema Electrónico de al Contraloría General de la República, SICE, y el Sistema Electrónico de Contratación Pública, SECOP, la creación de bases para un esquema de capacitación de funcionarios, la expedición de manuales de buenas prácticas para la gestión contractual así como la nueva normatividad de carácter reglamentario en materia de adquisiciones del Estado.
 - iii) La implementación del Sistema Electrónico de manuales de buenas prácticas para la gestión contractual así como de la nueva normatividad de carácter reglamentario en materia de adquisiciones del Estado
 - iv) La implementación del Sistema Electrónico de Contratación Pública, SECOP, avanza satisfactoriamente y a la fecha se reportan cerca de 2000 entidades estatales publicando información electrónica e incluso empezando a hacer subastas inversas por esa vía. El Sistema y sus módulos transaccionales se estima estén operando hacia mediados del 2009.
3. Numeral 3.37 Defense of the State: Es importante aclarar lo siguiente:
- i) La competencia de coordinación no son 200.000 salarios mínimos sino 2.000 salarios mínimos mensuales legales vigentes; y los 99.000 casos mencionados en el informe, no son los casos coordinados en el 2006 sino los consignados en el inventario que se obtuvo en el 2006 con el modulo de pleitos de la Nación. A diciembre de 2006 se pasó de cero casos coordinados en el 2002 a 2.129 coordinados.
 - ii) El sistema de información Litigiosa, Litigob, está en proceso de entrar en funcionamiento con la migración de la información disponible. Además el Ministerio del Interior y Justicia cuenta a la fecha con acceso al chip de la Contaduría General de la Nación sobre procesos judiciales contra el Estado.
 - iii) En lo que corresponde a la estimación del pasivo contingente de las demandas internacionales pro violación de derechos humanos y se está programando la segunda fase de valoración de esas demandas; mediante la definición de la metodología para valorar los laudos arbitrales.

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4. Numeral 3.7 Rut (Registro Único Fiscal, or Tax Registry), es importante ajustar el nombre del Rut pues no es Registro Único Fiscal sino Registro Único Tributario.

Agradecemos su atención. Cualquier información adicional no dude en contactarnos.

Cordialmente,

A handwritten signature in black ink, appearing to read 'Andrés Escobar Arango'.

ANDRES ESCOBAR ARANGO
Subdirector General

Copia: Doctora María Alejandra Gutiérrez, Subdirectora de Financiamiento, Organismos Multilaterales y Entidades Financieras Internacionales, MHCP
Doctor José Fernando Arias, Director de Desarrollo Social, DNP
Doctora Diana Vivas, Directora del Programa de Renovación de la Administración Pública, PRAP, DNP

Anexo: lo anunciado

Preparó: Carolina González

Revisó: Lina María Mondragón

Gestión de activos

El Gobierno definió y puso en marcha una política para la administración de activos que regula los procesos de inventario, titulación, adquisición, asignación y uso eficiente de los bienes del Estado. La gestión eficiente de los bienes inmuebles, por parte de las entidades del nivel central del Estado, ha permitido generar ahorros e ingresos. (Cuadro 1)

Cuadro 1
Ahorros e ingresos – Entidades activas y en liquidación
Resumen 2003- 2007

CONCEPTO	CAJA		AHORROS ESTIMADOS NO GENERAN CAJA		TOTAL AHORROS E INGRESOS \$	%	No. de INM.
	VENTA \$	RENTAS \$	OPERACIÓN Y MANTENIMIENTO \$	VALOR TRANSFERENCIA \$			
VENTAS	134.685.526.910	0	2.798.724.837	0	137.484.251.747	35,74%	1.051
VENTAS POR EL MARTILLO	71.851.563.173	0	1.947.522.188	0	73.799.085.361	19,18%	205
TRANSFERENCIA BIENES ENTRE ENTIDADES DEL ESTADO	0	0	8.109.578.684	1.653.656.000	8.109.578.684	2,11%	570
APORTE DE BIENES INMUEBLES PARA PROYECTOS DEL PND	0	0	182.782.322	0	182.782.322	0,05%	35
TRANSFERENCIA BIENES INMUEBLES A ENTIDADES TERRITORIALES	0	0	594.073.841	5.315.344.050	594.073.841	0,15%	57
CANCELACIÓN CONTRATOS DE ARRENDAMIENTO	0	0	1.866.737.009	0	1.866.737.009	0,49%	3
ARRENDAMIENTOS / CONCESIONES BIENES INMUEBLES CON PRIVADOS	0	132.075.163.131	15.836.192.556	0	147.911.355.686	38,45%	6.998
COMODATOS	0	0	14.764.809.689	0	14.764.809.689	3,84%	667
TOTAL ENTIDADES ACTIVAS	206.537.090.083	132.075.163.131	46.100.421.105	6.969.000.050	384.712.674.319	100,00%	9.586
VENTAS	258.540.065.896	0	1.906.511.745	0	260.446.577.641	89,99%	367
TRANSFERENCIA BIENES ENTRE ENTIDADES DEL ESTADO	0	0	21.544.106.405	111.070.609.000	21.544.106.405	7,44%	14.715
ARRENDAMIENTOS / CONCESIONES BIENES INMUEBLES CON PRIVADOS	0	2.746.289.386	3.420.372.442	0	6.166.661.828	2,13%	1.057
COMODATOS	0	0	1.266.482.831	0	1.266.482.831	0,44%	256
TOTAL ENTIDADES EN LIQUIDACIÓN	258.540.065.896	2.746.289.386	28.137.473.422	111.070.609.000	289.423.828.705	100,00%	16.395
TOTAL 2003-2007	465.077.155.979	134.821.452.517	74.237.894.528	0	674.135.503.024		25.981

NOTA: La información contenida en el cuadro es reportada por las entidades trimestralmente.

Fuente: DNP. Programa de Renovación de la Administración Pública – PROGA.

a) Estudio de Títulos:

Se ha realizado el estudio de títulos con fines de saneamiento jurídico de 4.135 bienes inmuebles de propiedad de las entidades del nivel central, incluida la revisión de 400 contratos de arrendamiento de los locales comerciales del Aeropuerto El Dorado, con el fin de dar apoyo en sus procesos de concesión que eventualmente se traducen en ingresos considerables para el Estado; 191 contratos de arrendamiento de la Caja de Retiro de las Fuerzas Militares (CREMIL); y 207 contratos de arrendamiento de IFI Concesión Salinas.

Frente a la meta establecida de 625 inmuebles jurídicamente saneados, el PROGA ha obtenido como resultado del seguimiento adelantando a los procesos emprendidos por las entidades, el saneamiento jurídico de 294 inmueble, lo que representa el cumplimiento del 47% de dicha meta.

b) *Inventario de Inmuebles:*

- Inventario de bienes inmuebles de entidades activas. A la fecha las entidades activas objeto del PROGA, han reportado un inventario de 10.067 bienes inmuebles (no incluye entidades en liquidación), de los cuales se han inspeccionado física y jurídicamente 9.181 de acuerdo con el Cuadro 2 que se presenta a continuación. Del total de los 9.181 bienes inmuebles, la información de 6.381 ha sido migrados al SIGA.

Cuadro 2
Entidades activas
Bienes inmuebles inspeccionados PROGA

Año	# de bienes inmuebles
2004	2.293
2006	2.888
2007	4.000
TOTAL	9.181

Fuente: DNP-PRAP-PROGA.

- Inventario de bienes inmuebles de entidades en liquidación. Las entidades en liquidación han venido reportando el inventario de sus activos inmobiliarios, a partir del año 2003, de acuerdo con el Cuadro 3 que se presenta a continuación.

Cuadro 3
Entidades en liquidación
Inventario de bienes Inmuebles reportados

AÑO	CANTIDAD INVENTARIO No.	VALOR INVENTARIO \$ millones	TRANSACCIÓN	
			INGRESOS \$ millones	AHORROS \$ millones
2.007	19.655	904.389	158.716	269
2.006	7.221	594.228	59.652	275
2.005	65.677	1.320.944	38.434	3.486
2.004	4.953	392.240	3.335	1.749
2.003	4.268	225.119	1.434	812
TOTALES ACUMULADO			261.571	6.591

Fuente: DNP-PRAP-PROGA.

La considerable variación que se presenta del 2004 al 2005, se debe a la inclusión de los bienes inmuebles que tenían algún tipo de anotación en los certificados de tradición y libertad a nombre del INURBE, los cuales no habían sido reportado ya que estaban en el proceso de cruzar las bases de datos con la Superintendencia de Notariado y Registro. Sin embargo, para el año 2007 se presentó nuevamente un incremento como resultado del cruce con las bases de datos de de las oficinas no sistematizadas de la Supernotariado, en todo el país.

A continuación se presenta un cuadro resumen a diciembre 31 de 2007 con el inventario, valor y gestión realizada por parte de estas entidades en liquidación, con el apoyo del PROGA, en el que se ha reducido el número de los bienes inventariados del cumplimiento de sus decretos en cuanto a la transferencia y/o venta de los bienes inmuebles.

Cuadro 4
Entidades en liquidación
Inventario y Gestión de bienes inmuebles 2007

Entidad	INMUEBLES INVENTARIADOS		INMUEBLES VENDIDOS		INMUEBLES TRANSFERIDOS		TOTAL INMUEBLES		PARA VENTA
	No.	Valor (\$ mill.)	No.	Valor (\$ mill.)	No.	Valor (\$ mill.)	No.	Valor (\$ mill.)	
INCORA	5.529	132.807	6	502	5.194	114.609	329	17.696	0
ALCALIS	2	628	1	133	0	0	1	495	0
INURBE	8.008	74.319	8	4.395	0	0	8.000	69.924	152
TELECOM	186	58.957	147	36.783	0	0	39	22.174	39
CAJANAL	36	43.204	26	29.027	9	0	1	14.177	0
FERROVIAS	5.718	236.787	10	67.758	795	138.285	4.913	30.744	0
ESE JOSÉ P. PADILLA	20	93.716	7	16.747	0	0	13	76.969	13
ESE URIBE URIBE	22	75.608	0	0	0	0	22	75.608	22
ADPOSTAL	97	23.108	0	0	0	0	97	23.108	97
ESE LUIS C. GALÁN	16	88.463	0	0	0	0	16	88.463	16
ESE POLICARPA S.	23	76.792	6	38.437	0	0	17	38.355	17
TOTALES	19.657	904.389	211	193.782	5.998	252.894	13.448	457.713	356

Fuente: DNP. Programa de Renovación de la Administración Pública – PROGA.

c) *Gestión:*

- Entidades Activas. A diciembre de 2007 se había obtenido el reporte promedio del 60% de las entidades objeto del PROGA, con ingresos y ahorros por \$ 160.036 millones (no incluye entidades en liquidación) con un porcentaje de cumplimiento del 160% de la meta establecida para el 2007. La información puede aumentar por envío tardío de la misma por parte de las entidades. (Cuadro 5)

Cuadro 5
Entidades activas
Resumen de ahorros e ingresos reportados año 2007

ÍTEM	No. DE ENTIDADES QUE REPORTAN	VALOR \$ millones	No. DE INMUEBLES
AHORROS E INGRESOS - 2007	60	\$ 160.036	2.983

Fuente: DNP - Programa de Renovación de la Administración Pública – Programa de Gestión de Activos.

- Entidades en liquidación. Las entidades en liquidación han venido reportando los ahorros e ingresos de sus activos inmobiliarios, a partir del año 2003, de acuerdo al Cuadro 6 que se presenta a continuación.

Cuadro 6
Entidades en liquidación
Resumen de ahorros e ingresos

CONCEPTO	2003	2004	2005	2006	2007	ACUMULADO
Ingresos (millones)	1.434	3.335	38.434	59.652	158.716	261.571
Ahorros (millones)	812	1.749	3.486	275	269	6.591
TOTAL	2.246	5.084	41.920	59.927	158.985	268.162

Fuente: DNP - Programa de Renovación de la Administración Pública – Programa de Gestión de Activos.