

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

BRAZIL

**FISCAL MANAGEMENT MODERNIZATION PROJECT FOR THE
STATE OF MATO GROSSO DO SUL
PROFISCO II – MS**

(BR-L1511)

**SIXTH INDIVIDUAL LOAN OPERATION UNDER THE
CONDITIONAL CREDIT LINE FOR INVESTMENT PROJECTS (CCLIP)
FISCAL MANAGEMENT MODERNIZATION PROGRAM IN BRAZIL – PROFISCO II**

(BR-X1039)

LOAN PROPOSAL

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ABBREVIATIONS

AWP	Annual work plan
CCLIP	Conditional credit line for investment projects
CEL	Comissão Especial de Licitação [Special Bidding Committee]
CGE/MS	Controladoria Geral do Estado de Mato Grosso do Sul [State of Mato Grosso do Sul Comptroller General's Office]
CGU	Controladoria Geral da União [Comptroller General of the Union]
COGEF	Comissão de Gestão Fazendária [Fiscal Management Commission]
CONEMAE	Coordenação do Núcleo Especial de Modernização da Administração Estadual [Coordination Office of the Special Unit for the Modernization of State Administration]
ECD	Escrituração contábil digital [digital bookkeeping]
EFD	Escrituração fiscal digital [digital tax accounting]
ESAF	Escola de Administração Fazendária [School of Finance Administration]
ENAP	Escola Nacional de Administração Pública [National School of Public Administration]
FADEFE/MS	Fundo de Apoio ao Desenvolvimento Econômico e de Equilíbrio Fiscal do Estado de Mato Grosso do Sul [Support Fund for the Economic Development and Fiscal Balance of the State of Mato Grosso do Sul]
IBGE	Instituto Brasileiro de Geografia e Estatística [Brazilian Institute of Geography and Statistics]
ICAP	Institutional Capacity Analysis Platform
ICMS	Imposto sobre a circulação de mercadorias e prestação de serviços [goods and services sales tax]
ICTs	Information and communication technologies
IEF	Instituto de Estudos Fiscais [Institute of Fiscal Studies]
IPEA	Instituto de Pesquisa Econômica Aplicada [Institute of Applied Economic Research]
IT	Information technology
LDO	Lei de Diretrizes Orçamentárias [Budgetary Guidelines Law]
LOA	Lei de Orçamento Annual [Annual Budget Law]
MD-GEFIS	Avaliação da Maturidade e Desempenho da Gestão Fiscal [Fiscal Management Maturity and Performance Assessment]
MEP	Monitoring and evaluation plan
MPDG	Ministry of Planning, Development, and Management
MS	State of Mato Grosso do Sul
NF-e	Nota fiscal eletrônica [electronic tax invoice]
PCU	Project coordination unit
PEP	Program execution plan
PGE/MS	Procuradoria Geral do Estado de Mato Grosso do Sul [State of Mato Grosso do Sul Attorney General's Office]
PMR	Progress monitoring report

PNAFE	Programa Nacional de Apoio à Modernização da Administração Fiscal para os Estados Brasileiros [National Fiscal Administration Program for the Brazilian States]
PNAFM	Programa Nacional de Apoio à Gestão Administrativa e Fiscal dos Municípios Brasileiros [Fiscal Management Program for Brazilian Municipalities]
PPA	Plano Plurianual [Multiyear Plan]
PROFISCO	Programa de Apoio à Gestão e Integração dos Fiscos no Brasil [Program to Support the Management and Integration of Finance Administrations in Brazil]
SAD/MS	Secretaria de Estado de Administração de Mato Grosso do Sul [State of Mato Grosso do Sul Department of Administration]
SEFAZ/MS	Secretaria de Estado de Fazenda de Mato Grosso do Sul [State of Mato Grosso do Sul Department of the Treasury]
SEGOV/MS	Secretaria de Estado de Governo e Gestão Estratégica de Mato Grosso do Sul [State of Mato Grosso do Sul Department of the Interior and Strategic Management]
SPED	Sistema Público de Escrituração Digital [Digital Public Accounting System]
SPF	Sistema de Planejamento e Finanças [Planning and Finance System]
STN	Secretaria do Tesouro Nacional [National Treasury Department]
TCE/MS	Tribunal de Contas do Estado de Mato Grosso do Sul [State of Mato Grosso do Sul Audit Office]

PROJECT SUMMARY

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Financial Terms and Conditions						
Borrower: State of Mato Grosso do Sul			Flexible Financing Facility^(a)			
Guarantor: Federative Republic of Brazil			Amortization period:	25 years		
Executing agency: State of Mato Grosso do Sul, acting through its Department of the Treasury (SEFAZ/MS)			Disbursement period:	5 years		
			Grace period:	5.5 years ^(b)		
Source	Amount (US\$)	%	Interest rate:	LIBOR-based		
IDB (OC):	47.7 million	90%	Credit Fee:	(c)		
Local:	5.3 million	10%	Inspection and supervision fee:	(c)		
Total:	53.0 million	100%	Weighted average life (WAL):	15.25 years ^(d)		
			Currency of approval:	United States dollars		
Project at a Glance						
<p>Project objective/description: The project objective is to contribute to the state’s fiscal sustainability through: (i) modernization of fiscal management; (ii) improvement of tax administration; and (iii) improvement of public expenditure management. This project is the sixth individual loan operation under the PROFISCO II CCLIP (BR-X1039) approved by the Board of Executive Directors through Resolution DE-113/17.</p>						
<p>Special contractual conditions precedent to the first disbursement of the loan proceeds: (i) The borrower will adhere to the program Operating Regulations previously approved by the Bank for all individual operations under the PROFISCO II CCLIP; and (ii) the project coordination unit (PCU) will be established, and its members appointed (see paragraph 3.4). For other contractual conditions precedent to the first disbursement of the loan proceeds of a fiduciary nature, see in Annex III, paragraph 4.1.</p>						
<p>Special contractual condition for execution: Prior to the start of activities whose beneficiaries will be the State of Mato Grosso do Sul Department of the Interior and Strategic Management (SEGOV/MS), Department of Administration (SAD/MS), Comptroller General’s Office (CGE/MS), and Attorney General’s Office (PGE/MS), the executing agency will sign cooperation agreements with those entities to establish the roles and responsibilities of the parties as part of program execution (see paragraph 3.5).</p>						
Exceptions to Bank policies: None.						
Strategic Alignment						
Challenges:^(e)	SI	<input type="checkbox"/>	PI	<input checked="" type="checkbox"/>	EI	<input type="checkbox"/>
Crosscutting themes:^(f)	GD	<input type="checkbox"/>	CC	<input type="checkbox"/>	IC	<input checked="" type="checkbox"/>

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

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

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

^(d) The weighted average life (WAL) may be less than stipulated, depending on the signature date of the loan contract.

^(e) SI (Social Inclusion and Equality); PI (Productivity and Innovation); and EI (Economic Integration).

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

I. DESCRIPTION AND RESULTS MONITORING

A. Background, problem to be addressed, and rationale

- 1.1 This project is the sixth individual loan operation under the PROFISCO II conditional credit line for investment projects (CCLIP) (BR-X1039), approved by the Board of Executive Directors through Resolution DE-113/17, which the Government of Brazil has requested from the Bank¹ with a view to consolidating the progress made by the PROFISCO I CCLIP (BR-X1005) and to continue modernizing the states' fiscal management.
- 1.2 The purpose of PROFISCO I was to promote the integration of tax administrations in Brazil and to modernize the fiscal, financial, and property management of the states by instituting the Digital Public Accounting System (SPED) using the electronic tax invoice (NF-e).²
- 1.3 **Economic and fiscal features of Brazil.** Brazil is facing significant challenges in keeping its economy on a sustainable growth path. Its GDP contracted 3.8% in 2015, and 3.5% in 2016, and grew 1.1% in 2017 ([IBGE, 2018](#)). The economy is expected to continue growing in the medium term, with projected growth of 1.9% for 2018 and 2.1% for 2019.³
- 1.4 The decline in economic activity caused the consolidated public sector revenue to fall significantly, representing around two percentage points of national GDP between 2013 and 2016 ([World Economic Outlook](#), IMF, 2017). Despite the downward trend in tax revenue intake, public expenditure climbed steadily over this period from 37.4% of national GDP in 2013 to 41.6% in 2016. Consequently, the primary balance has deteriorated in recent years, in comparison with previous periods, from an average primary surplus of 3.4% of national GDP in 2002-2008, to 1.3% in 2009-2015. In 2016, the primary deficit reached 2.5% of national GDP,⁴ and the country is not expected to run a structural primary surplus again until 2019 ([IMF, 2017](#)). Public debt in relation to national GDP also rose by almost one third over three years, from 60.2% of national GDP in 2013 to 78.3% in 2016, and is projected to reach 81.2% by 2021 ([IFI, 2017](#)).
- 1.5 The recessionary setting has also adversely impacted the fiscal performance of the Brazilian states. State tax revenue intake shrank from 7.6% of national GDP in 2008 to 6.9% in 2015. The goods and services sales tax (ICMS), which is the states' main source of tax revenue, declined by an average 6% in real terms from 6.7% of national GDP in 2013 to 6.5% in 2015. Moreover, federal government transfers to the states lessened over this same period from 2.9% of national GDP to 2.5% ([STN, 2016](#)).

¹ [Letter from the Ministry of Finance](#). The project has a favorable recommendation from the External Financing Commission (COFIEX), [No. 03/0122](#), and [state legislative approval](#).

² [McKinsey & Co., 2014](#). The NF-e and SPED increased the risk of detection of tax evasion and helped to reduce employment informality in Brazil over the last 10 years (from 55% to 40%).

³ [IMF, 2018](#). The 5 February 2018 [Focus](#) market report of the Central Bank of Brazil projects GDP growth of 2.7% for 2018 and 3% and 2019.

⁴ Macroeconomic volatility forced the authorities to revise the primary balance targets in fiscal 2016 and 2017 ([IFI, 2017](#)).

- 1.6 As state revenues weakened, current expenditure climbed steadily, driven by rising personnel costs, which went from 10.2% of national GDP in 2011 to 10.9% in 2015 ([Rossi, 2016](#)). Investment fell by 16% on average in real terms in 2013-2016. Thus, the primary balance began to deteriorate in 2012, recording primary deficits in three of the last four years. In 2016, 10 of the 27 states ran primary deficits ([STN, 2017](#)).
- 1.7 **Public finances of Mato Grosso do Sul (MS).** The lower level of activity in the Brazilian economy has led to a decline in the nominal growth rate of state GDP, which fell from 14% in 2014 to 5% in 2015 ([IBGE, regional GDP 2002-2015](#)). As a result, the real annual growth rate of tax revenues dropped from 6% between 2010 and 2014 to -3.1% in 2015-2016, before returning to positive growth in 2017. The proceeds of the ICMS shrank from a real annual growth rate of 5.6% to -5.3% over the same period, reducing its share of state GDP from 9% in 2013 to 8.4% in 2015.⁵
- 1.8 To address this decline in revenues, the state of MS took steps to contain current expenditure,⁶ and the payroll costs of the executive branch consequently went from representing 47.23% of net current revenues in 2014, which was above the prudential limits of the Fiscal Responsibility Law, to 43.15% in 2016 ([STN, 2018](#)). The real annual growth rate of investment expenditure shrank from 8.2% in 2010-2014 to -27.9% in 2015-2016, cutting the state's investment in 2016 to the equivalent of half what it was in 2010, in real terms.⁷
- 1.9 In the period 2013-2014, the primary balance was negative on average at 0.4% of state GDP, although it recovered in 2015 and 2016 to an average surplus of 1%. The consolidated debt went from 120% of net current revenues in 2013 to 100% in 2016 ([STN, 2018](#)).
- 1.10 **Rationale.** The national and state macroeconomic contexts highlight the need for further measures to modernize fiscal management in MS, with a view to keeping the public accounts in balance and consolidating the state's fiscal sustainability. In [PROFISCO I – MS](#), the emphasis was on improving tax administration by promoting: (i) integration of the state tax administration with other levels of government through introduction of the SPED; and (ii) improving enforcement and collection capabilities through the development of systems and access to virtual services for taxpayers. This project, in addition to reinforcing efforts at modernization under the first phase, will promote: (i) the strengthening of public expenditure management; (ii) use of the SPED and digital technologies to enhance tax intelligence, electronic auditing, enforcement, public procurement, and other areas; and (iii) simplification of tax compliance to make the state more competitive.
- 1.11 The effectiveness and efficiency of public institutions are limited by the restrictions faced by their staff in terms of access to information technologies, the availability of financial resources, and the legal framework (Arenas de Mesa, 2016; Finan et al., 2017). MS needs to address lingering weaknesses in staffing that limit its fiscal

⁵ Fiscal Data, SEFAZ/MS.

⁶ [Public expenditure ceiling](#). Accession to the Ministry of Finance plan for assistance and stimulus measures to restore the fiscal balance of the states ([Supplemental Law 156/2016](#)) through renegotiation and extension of their debt profile with the federal government, audits and improved payroll management, and an [administrative restructuring of the state government](#).

⁷ [Fiscal Data, SEFAZ/MS](#).

- performance. In terms of human resources,⁸ the State of Mato Grosso do Sul Department of the Treasury (SEFAZ/MS) has 1,192 headcount staff and 46 contractors. In terms of planning and managing its human resources, the department lacks information, professional performance evaluation methodologies, and procedures for resizing the labor force and quantifying skills. Although 80% of its personnel has a higher education, there are few training offerings for the maintenance and further development of professional qualifications. The total average budget of SEFAZ/MS in 2013-2016 was US\$17.5 million, 60% earmarked for payroll and 40% for investments, but less than 1% for training. In addition, SEFAZ/MS has no code of ethics for its employees, although there are standards of conduct and an ethics commission in place.⁹
- 1.12 In terms of access to technologies, the SEFAZ/MS technology platform is inadequate to meet the need to protect and retrieve data and information and ensure its integrity, and to meet demand for new technologies and the processing of large volumes of data. There are also weaknesses, restrictions, and obsolescence in the network, server, and system monitoring software that cause delays in response times and longer processing times for services. SEFAZ/MS currently administers 10,115 workstations, 6,018 of which have been in use for more than four years and have low processing power. The SEFAZ/MS information and communication technology (ICT) area is responsible for maintaining all [354 computer systems of the state](#), 198 of which are specific to SEFAZ/MS (29 of these systems run on obsolete platforms).¹⁰
- 1.13 In terms of the legal framework, the rules for granting and tracking tax concessions (exemptions) are tenuous. This reflects the inadequacy of controls and shortcomings in the systems. There is no automatic management of the 3,541 firms that benefit from tax exemptions.
- 1.14 There are other significant challenges to strengthening the fiscal sustainability of MS that were identified using the evaluation methodology of [the Fiscal Management Maturity and Performance Assessment](#) (MD-GEFIS),¹¹ the Report on Implementation of the Institutional Capacity Analysis Platform (ICAP),¹² and the [Matrix of Problems, Solutions, and Results](#), which is the instrument for defining outputs and activities based on the identified problems and challenges, as described below.
- 1.15 Weaknesses in **fiscal management** adversely affect the institutional performance of SEFAZ/MS, as a result of:

⁸ Human Resources, SEFAZ/MS.

⁹ [State Law 2.195/2000](#).

¹⁰ [ICT report, SEFAZ/MS](#).

¹¹ [Evidencias evaluación MD-GEFIS MS](#) [Evidence for MD-GEFIS evaluation MS].

¹² This report indicated that SEFAZ/MS has medium execution capacity, given its extensive experience in the execution of projects in its sector using its own staff for implementation. It was identified that the SEFAZ/MS has institutional capacity in all areas assessed: legal framework and governance, human resources and managerial and technical capabilities, project administration, procurement management, and financial management.

- a. **Poor alignment between fiscal management and other areas of government to support the strategic actions and scope of the agreed institutional outcomes**, due to the following: (i) the agreed indicators in the strategic plan are misaligned with government priorities¹³ and not systematically revised; (ii) there are no methodologies for managing processes and projects, with no method for setting priorities, allocating resources, and managing risks; (iii) the strategic management processes are obsolete, and there is no integration with the government's corporate systems; (iv) there is cultural resistance to the monitoring and control of processes and projects; and (v) physical space is inadequate.
- b. **There are still few correction, audit, and control measures in place**, due to the following: (i) there are no rules for implementing the guidelines approved in [Law 230/2016](#) on correction, audit, and control of the state; (ii) there are no procedures for standardized internal control, which is limited to occasional inspections;¹⁴ (iii) there is no information for monitoring public expenditure actions, as recommended by the Comptroller General of the Union (CGU);¹⁵ and (iv) training is not skills-based.
- c. **The workforce is being used inefficiently¹⁶ to achieve SEFAZ/MS corporate results**, due to the following: (i) job assignment, transfer and promotion to management are not based on criteria of merit, performance,¹⁷ and innovation and are untied to SEFAZ/MS strategic directives;¹⁸ (ii) there is a lack of knowledge about individual skills for reducing skills gaps; (iii) human resources are distributed without corporate competency-based management criteria; (iv) training offerings have little to do with the required skills; (v) there is a lack of methodologies for knowledge creation, capture, and sharing at SEFAZ/MS; and (vi) there is little sharing of knowledge or dissemination of good practices, due to the lack of modern tools.
- d. **There is little control over personnel expenditure**, due to the following: (i) there are inefficiencies in the control of personnel expenditure, including no cross-referencing of information on employees;¹⁹ and (ii) corporate systems are unintegrated and inconsistent with rules under existing legislation (for example, [e-Social](#)), leading to delays²⁰ and the manual data entry.
- e. **The capacity for generating ICT products and services is insufficient to meet modernization/innovation needs**, due to the following: (i) there are no

¹³ In its [strategic map](#), the state established 152 initiatives and 12 management contracts, 101 of which were completed: [Management Contract Evaluation Report 2017, SEGOV/MS](#).

¹⁴ [Sixty-five audit reports, 2017, CGE/MS](#).

¹⁵ [Technical Cooperation Agreement 4](#).

¹⁶ SEFAZ/MS workforce: 1,238 employees, 998 with higher education degrees, 218 with high school education, and 22 with basic education.

¹⁷ [Regulations for individual performance evaluation of MS public employees](#).

¹⁸ [Guidelines for the introduction of competency-based management](#).

¹⁹ In 2016, 39% of temporary teachers had actually been in place more than two years, longer than stipulated by law.

²⁰ Actual time for processing payroll data in the state's computer system (monthly): 30 hours.

guidelines, planning, monitoring, and evaluation of ICT management; (ii) there are no contingency procedures in the event of failures and disasters, and data communication performance is poor; (iii) there are no rules and regulations in place for ICT management and security processes; (iv) state information is vulnerable; (v) the hardware structured is insufficient in terms of both disk space and memory and processing capacity;²¹ (vi) there is little standardization of ICT services; (vii) there are no instruments for dealing with contingencies in the event of failures and disasters, and data communication performance of fiscal units is poor; (viii) many [ICT service request](#) and [helpdesk](#) calls go unanswered; and (ix) systems use outdated computer languages, and ICT equipment is obsolete and runs on outmoded platforms.

- f. **Low level of communication with the public:**²² (i) there is no evidence of the impact of the fiscal education program instituted in 2000; (ii) the guidelines for fiscal education²³ are out of date and technologically obsolete; (iii) there is little interaction or responsiveness to citizen requests for information;²⁴ and (iv) information is incomplete, fragmented, or inconsistent due to the limited interaction with state systems and databases.

1.16 **In the tax administration the degree of tax evasion is still high, which affects the performance of revenue collection.** Tax evasion in Brazil represents an estimated 7.6% of GDP.²⁵ This is a consequence of:

- a. **Inefficient management of tax concessions:** (i) the granting of tax concessions is fragmented among areas of government; (ii) the processes for granting tax concessions is not tied to a government strategy;²⁶ (iii) there is no methodology for economic analysis (costs and benefits) of tax expenditures in the short and medium term; (iv) decisions are made subjectively due to scattered data and lack of management reports quantifying tax expenditure in relation to revenues; and (v) there is no unified tool for the government to interact with the private sector on the state's development policy.
- b. **Complexity in compliance with tax obligations,** due to: (i) the low reliability of tax roll data results in transaction costs for the taxpayer and the tax administration,²⁷ caused by: (a) fragmented use of the database, inconsistency in replicating tax roll data, and a taxpayer registry that is out of date; (b) little or no integration of information with other state, municipal, and federal agencies; and (c) primarily manual changes to the tax roll that need to be integrated with

²¹ The storage capacity of SEFAZ/MS is 613.7 terabytes, with 90.6% of that capacity established, and the [availability rate of the data center](#) in 2017 was 92%, equivalent to 720 hours per year of unavailability, which is below the minimum level established by the TIER 1 standard (Telecommunications Infrastructure Standard for Data Centers), which is 99.87%, equivalent to 28 hours per year of unavailability.

²² [Instituto PUBLIX](#), 2015. On the Transparency and Fiscal Citizenship Index for the Brazilian states, MS was rated zero for direct communication with citizens.

²³ [Fiscal Education Portal](#).

²⁴ [MS Government Transparency Portal](#) and [visits to the Transparency Portal in 2017](#).

²⁵ [SINPROFAZ](#), 2016, "Sonegação no Brasil – Exercício 2015" [Tax Evasion in Brazil, Fiscal Year 2015].

²⁶ [Legislation governing tax concessions, SEFAZ/MS](#).

²⁷ In 2017, 1,784 taxpayers had their registrations canceled, resulting in the improper rejection of 12,645 electronic documents: SEFAZ/MS.

other subsystems; (ii) the additional operating cost to taxpayers of complying with redundant ancillary obligations²⁸ such as the requirement to file returns with redundant information in relation to the digital tax accounting record (EFD); and (iii) the means of tracking tax obligations in relation to foreign trade are inefficient due to limited tracking of foreign trade transactions by the state, creating additional costs to the taxpayer as a result of substantial documentation requirements.

- c. **Limited efficiency and effectiveness of tax enforcement measures, undermining tax revenue intake**, due to the following: (i) the stages involving fiscal planning, taxpayer selection, audits, and the compilation of results are conducted in a decentralized manner that is not systematic or integrated; (ii) the tools used for inspection and audit are obsolete, as a result of which: (a) planning is done manually without a methodology; (b) taxpayer selection is from nonsystematic tax bases using nonparameterized criteria that are not integrated with the system for issuing audit orders;²⁹ (c) laws and regulations contain no procedures for self-regularization; (d) there are no mechanisms for tracking and supporting the execution and results evaluation of planned actions; and (e) there is no tool for identifying, calculating, and notifying taxpayers of their taxes; (iii) inspections of goods in transit are obsolete, based on the mandatory stopping of all vehicles;³⁰ (iv) there is no preprocessing of electronic documents used in inspections; (v) infrastructure is weak with little automation, which hinders comprehensive, real-time tracking of freight; (vi) tax intelligence activities are deficient; (vii) taxpayer compliance findings are controlled without any method of analysis and data processing; and (viii) data for identifying tax fraud rings are not integrated among government agencies.
- d. **Inefficient handling of tax litigation with long completion times for proceedings**,³¹ due to the following: (i) the tax litigation model is out of date, burdensome, and complex; and (ii) the tax litigation process is manual and unstandardized, producing a high risk of losing cases, and taxpayer access is limited.
- e. **Eroding services to taxpayers**, due to the following: (i) taxpayer service procedures are not standardized; (ii) taxpayer requests and complaints are processed physically;³² (iii) the level of taxpayer satisfaction with SEFAZ/MS services is unknown; and (iv) there are no automated tools for managing and consulting legislation.
- f. **Low rate of recovery assessed tax owed, both administrative and via the courts**,³³ due to the following: (i) processes in the areas of recovery, collection, tax refunds, and tax claims are fragmented and obsolete; (ii) the tax collection system does not issue management reports, nor is it integrated with other

²⁸ [Estimated cost of tax return intake, SEFAZ/MS.](#)

²⁹ In 2016, 2,069 flawed orders were issued, impacting 5,378 taxpayers, SEFAZ/MS.

³⁰ 100% of vehicles are inspected physically.

³¹ Average processing times in SEFAZ/MS: trial level, 172 days; appeal level, 470 days.

³² [Catalogue of SEFAZ/MS services.](#) Of 144 [services to taxpayers](#), only 48 are fully online.

³³ [Recovery of assessed tax owed, 2015-2017, SEFAZ/MS.](#)

systems of the state and other levels of government; (iii) the analysis and tracking of tax payment returns is done manually, and not integrated; (iv) the tax claim process is outmoded, and proof of tax claims must be presented in person; and (v) the tax claim system does not issue management reports and is not integrated with other state systems.

1.17 The administration of public expenditures lacks effective instruments to generate reliable and timely budgetary, financial, and asset management information for decision-making and optimization of the use of public resources. This is a consequence of:

- a. **Inefficient allocation of resources in public policies**³⁴ and limited responsiveness for decision-making, due to the following: (i) the scant interaction among corporate systems in the areas of planning, budgeting, and strategic management limits realistic estimates of revenues and expenditures; (ii) there are no flows or procedures defining budgetary, financial, and accounting management; (iii) there are no methodologies for simulating the short and medium-term fiscal impact in contracting new credit operations and public-private partnerships; and (iv) the [instruments for planning the stages of the MS fiscal cycle](#) are weak. The Brazilian Public Sector Accounting Standards and Public Sector Accounting Manual are not fully applied.
- b. **Inefficient procurement management**, due to the following: (i) the effectiveness of state procurement procedures is unknown;³⁵ (ii) there are no defined procedures nor any computerized system for monitoring and enforcing contracts and agreements, and each administrative unit does this independently; and (iii) there is a lack of technical knowledge for conducting state procurement processes.
- c. **Inefficient pension management, resulting in financial losses to the state**, due to the following: (i) documentation prior to 1989 is incomplete and poorly organized, and there is no tracking of procedures and the payment of benefits; (ii) the tracking and management of the granting of pensions, re-evaluations, certificates, accounting, finances, assets, and registries are compiled manually;³⁶ (iii) there is no cross-referencing of data for government decision-making; (iv) the registry of retirees and pension recipients is out of date;³⁷ and (v) public servants have limited qualifications in pension management.
- d. **Inefficient management of investment expenditure**, due to the following: (i) investment projects are defined by demand, with no criteria for setting priorities based on technical qualifications; (ii) the state does not have an up-to-date public investment portfolio;³⁸ (iii) the [existing legal framework](#) has not been revised to ensure greater legal safeguards for public-private partnerships; (iv) public and private agents have only limited knowledge of state investments;

³⁴ [Frequent reallocation of resources during budget execution \(2014-2017\)](#). SEFAZ/MS.

³⁵ [Solicitations issued in 2017](#), SAD/MS. 782 direct contracting awards, giving rise to 103 audit notifications.

³⁶ Average time for granting retirement requests: 120 days. SAD/MS.

³⁷ The 2016 census of pension recipients yielded monthly savings of 241,859.99 Brazilian reais. SAD/MS.

³⁸ There is no portfolio of investment projects, only a [portfolio of projects](#). SEFAZ/MS.

(v) there are no guidelines, standards, or methodologies for trimming the costs of investments; (vi) cost breakdown information is scattered; and (vii) there are no sector studies analyzing the costs of public services.³⁹

- 1.18 **The Bank's experience in the country.** The Bank has financed programs to improve fiscal management in Brazil, particularly at the state level, under the National Fiscal Administration Program for the Brazilian States (PNAFE) (loan 980/OC-BR) and the PROFISCO I CCLIP (BR-X1005). It has also supported the Fiscal Modernization Project in the State of São Paulo, the Program to Support Fiscal Management Modernization and Transparency in the State of Bahia (loan 1727/OC-BR) and the fiscal stability consolidation projects in the states of Amazonas, Alagoas, Bahia, Pernambuco, and Rio Grande do Sul.⁴⁰ At other levels of government, the Bank has supported the Federal Revenue Service Fiscal Modernization Program (SRF) (1996), and the Fiscal Management Program for Brazilian Municipalities (PNAFM I, loan 1194/OC-BR; PNAFM II, loan 2248/OC-BR; and PNAFM III, loan 3391/OC-BR).
- 1.19 According to the [midterm evaluation of the PROFISCO I CCLIP \(2014\)](#), between 2009 and 2013 the states with a PROFISCO program in the advanced stage of execution recorded revenues from the goods and services sales tax (ICMS) that were on average 6% higher than those of states where the PROFISCO program was in the early stages of execution. According to the [final progress report, the PROFISCO I – MS operation](#) was implemented in a satisfactory manner, achieving 83% of the impact indicators and 89% of the outcomes originally planned.⁴¹
- 1.20 **Lessons learned.** The lessons learned from the PROFISCO I CCLIP and the PROFISCO I – MS operation include the following:
- a. **Design.** An instrument is needed to identify innovative solutions in fiscal management processes. The Fiscal Management Maturity and Performance Assessment (MD-GEFIS), which identifies the maturity of the state's fiscal management processes and opportunities for strengthening them, was developed for this purpose.⁴²
 - b. **Development.** The participation of SEFAZ/MS in the network of the [Fiscal Management Commission](#) (COGEF) encouraged the exchange of know-how and solutions with other states for fiscal management modernization.
 - c. **Execution.** To overcome execution delays, the Bank created a monitoring tool called the Accelerated Execution Plan which uses the progress monitoring report (PMR) to identify outputs that are late and prepare mitigation measures to get them back on track.
 - d. **Outcomes.** It was found that the SPED, including the NF-e, EFD, and digital bookkeeping (ECD), were the outputs making the biggest contribution to

³⁹ The [fiscal adjustment program](#) calls for implementation of a costing system.

⁴⁰ Policy-based loan programs: 2081/OC-BR; 2841/OC-BR; 2850/OC-BR; 3039/OC-BR; 3061/OC-BR; 3138/OC-BR; and 3139/OC-BR.

⁴¹ Loan 2327/OC-BR, PMR.

⁴² [CIAT, June 2017. MD-GEFIS: A proposal for evaluation.](#)

increasing the efficiency of state tax audits.⁴³ This operation will invest in the SPED's development and seek to maximize its potential by expanding the use of the information it generates to automate tax auditing,⁴⁴ simplify tax obligations, and improve public procurement ([CONSAD, 2016](#)), etc., by leveraging new digital economy technologies.

- e. PROFISCO I – MS, specifically, obtained a 24-month extension of the execution period. The negative factors were found to cluster around: (i) a change of decision in implementing the integrated fiscal management system that was to be donated by the State of Pernambuco, given the technological platform's architecture and the high cost of maintaining the system; (ii) the short time frame for execution of the 20 outputs (four years); and (iii) a delay in the Bank's accreditation of the state's e-procurement management system. These lessons have been reflected in the PROFISCO II – MS operation, which will have fewer outputs (16), use the state's electronic exchange, require cooperation agreements between SEFAZ/MS and the agencies involved, and have an execution period of five years.
- 1.21 **The Bank's international experience in other countries of the region.** Recent Bank experience with tax administration reform in Jamaica (loan 2658/OC-JA), Ecuador (loan 3325/OC-EC), Honduras (loan 3541/BL-HO), Peru (loan 3214/OC-PE), El Salvador (loan 3852/OC-ES), and Guatemala (loan 3786/OC-GU), as well as with modernization of financial administration systems in Honduras (loan 2032/BL-HO), Guatemala (loans 2050/OC-GU and 2766/OC-GU), and Guyana (loans 1550/SF-GY and 1551/SF-GY), have been reflected in this operation, which also emphasizes the role of institution-strengthening and fiscal management modernization, and some of the [lessons learned](#).
- 1.22 **The Bank's country strategy.** The project is aligned with the Bank's country strategy with Brazil 2016-2018 (document GN-2850) in relation to the objective of improving the business climate and enhancing efficiency in the management of public resources. The operation is also included in the 2018 Operational Program Report (document GN-2915).
- 1.23 **Strategic alignment.** The project is consistent with the Update to the Institutional Strategy 2010-2010 (document AB-3008), and strategically aligned with the development challenge of productivity and innovation through reducing tax collection costs,⁴⁵ and with the crosscutting area of institutional capacity and rule of law, through the strengthening of tax systems⁴⁶ and public resource management and planning systems.⁴⁷ The project contributes to the Corporate Results Framework 2016-2019 (document GN-2727-6) via the indicators for: (i) percent of GDP collected in taxes; and (ii) government agencies benefited by projects that strengthen technological and managerial tools to improve public service delivery, through

⁴³ [McKinsey & Co., 2014](#).

⁴⁴ The use of the SPED and artificial intelligence will broaden the identification of tax fraud. See [Araujo, 2013](#).

⁴⁵ Outcome indicator 2 of the Results Matrix.

⁴⁶ Impact indicator 2 and component II output indicators of the Results Matrix.

⁴⁷ Outcome indicator 3 and component III output indicators of the Results Matrix.

strengthening of the e-Fisco; (iii) accountability institutions strengthened; and (iv) subnational governments benefited by decentralization, fiscal management, and institutional capacity projects. Lastly, it is aligned with the Sector Strategy on Institutions for Growth and Social Welfare (document GN-2587-2), and consistent with the sector frameworks documents on Decentralization and Subnational Governments (document GN-2813-3), and Fiscal Policy and Management (document GN-2831-3) under the dimensions of: (i) improving the efficiency and quality of expenditure and service delivery; (ii) improving own revenue collection; and (iii) working with greater transparency and accountability.

B. Objectives, components, and cost

- 1.24 The project objective is to contribute to the state's fiscal sustainability through: (i) modernization of fiscal management; (ii) improvement of tax administration; and (iii) improvement of public expenditure management.
- 1.25 Enhancing the performance of public finance, increasing tax revenue intake, increasing the efficiency of public expenditure, and thus strengthening the fiscal sustainability of the State of Mato Grosso do Sul (MS) will benefit its citizens, corporate and individual taxpayers, as well as public and nongovernmental sector entities through better service delivery, ease and lower cost of tax compliance, and greater availability of information and data for public management and transparency of public accounts. This operation will finance the following components:
- 1.26 **Component I. Fiscal management and transparency (US\$26,475,200).** This component seeks to improve management instruments, modernize technological infrastructure, and improve the relationship with taxpayers. It will finance:
- a. **Implementation of a public fiscal governance model**⁴⁸ through: (i) updating of the government's strategic plan, including an institutional indicator dashboard; (ii) introduction of a methodology for managing processes and projects, including risk management, aligned with government directives; (iii) redesign and automation of strategic management processes with the integration of corporate systems; (iv) implementation of the internal communication plan; and (v) physical upgrades to the working environment of SEFAZ/MS.
 - b. **Implementation of the state comptroller model**⁴⁹ through: (i) design of the operational model for compliance, audit, and public hearings based on performance, quality, and risk analysis; (ii) implementation and automation of internal processes of the Comptroller General's Office, integrated into the state's strategic management system; (iii) methodology for processing data on public spending, in order to expand efforts to prevent and combat corruption; and (iv) a training plan for the State of Mato Grosso do Sul Comptroller General's Office (CGE/MS).
 - c. **Implementation of a model for skills-based strategic personnel management**⁵⁰ through two suboutputs: (i) a skills-based training plan,

⁴⁸ [Fiscal governance model.](#)

⁴⁹ [State comptroller model.](#)

⁵⁰ [Model for skills-based strategic personnel management.](#)

containing (a) definition of the skills-based management methodology aligned with the strategic objectives of SEFAZ/MS; (b) mapping of individual skills and analysis of the job description, the skills gap, and the dimensioning of the work force; (c) Individual Development Plan, with criteria for the recognition of performance; (d) implementation of the annual training plan; and (e) physical upgrade of multimedia spaces; and (ii) knowledge management tools with: (a) definition of the knowledge management methodology; and (b) introduction of knowledge tools (library, historical archives, databank of ideas and talent).

- d. **Implementation of a payroll management system**⁵¹ through: (i) definition of a payslip management model, including electronic audit routines; and (ii) upgrade and integration of the pay slip system with the state's corporate systems for planning, finance, and granting of benefits, generating information for e-Social and the state employee performance management cycle.
 - e. **Implementation of an ICT management and operations model**.⁵² This includes two suboutputs: (i) ICT management and security plans, with: (a) preparation of an ICT and information security master plan; (b) mapping, documentation of internal ICT management and security processes and preparation of a catalog of services; and (c) upgrade of the system for ICT request handling and tracking (service desk); and (ii) ICT platforms, with: (a) expanded capacity for processing, storing, and transferring data from the data center; (b) updating of microcomputer hardware; (c) expanded and improved security and performance of the local, remote, and metropolitan-area data networks; (d) implementation of a unified platform for identity management, systems integration, and management of integrations and electronic processing solution; (e) implementation of data contingency platform; (f) installation of network operations management and monitoring tools; (g) implementation of new ICT solutions using artificial intelligence; and (h) implementation of tools for handling large volumes of data ("Big Data").
 - f. **Implementation of the Web-based platform for transparency and fiscal citizenship**⁵³ through two suboutputs: (i) fiscal education plans, with (a) evaluation of fiscal education actions, and (b) implementation of the fiscal education plan using new technologies; and (ii) tools for communicating with citizens, through: (a) updating of the citizen information system and (b) implementation of a Web-based transparency portal and multifunctional software.
- 1.27 **Component II. Tax administration and litigation (US\$15,206,000).** This component seeks to grow internally generated revenues and simplify tax compliance. It will finance the following activities:
- a. **Implementation of a system for managing tax concessions**⁵⁴ through: (i) mapping of the tax concession grant and control process; (ii) definition of a methodology for managing tax concessions; (iii) definition of a methodology for

⁵¹ [Payroll management system.](#)

⁵² [ICT management and operations model.](#)

⁵³ [Transparency and tax compliance.](#)

⁵⁴ [Tax concessions.](#)

analyzing tax concessions and their economic impact; (iv) introduction of a system for managing tax concessions with management reports; and (v) implementation of a virtual development agency for interaction between government and the private sector.⁵⁵

- b. **Implementation of simplified tax obligations systems (mandatory outputs)**⁵⁶ through (i) a single taxpayer registry, covering: (a) update and adjustment of state agencies' taxpayers registries to reflect the needs of the various user systems; (b) adaptation of the registration system for immediate state registration (or denial of registration, if warranted); and (c) a technological solution for automatic cancellation of state registration simultaneous with removal from the commercial registry; (ii) consolidation of SPED/EFD ancillary tax obligations, including: modules for analyzing data from the "Information and calculation guide: Tax substitution" and "Information and calculation guide: Tax concession in the EFD from the ICMS; and (iii) integration into the international trade single window, including implementation of the export and import control system.
- c. **Implementation of systems for inspection and tax intelligence.**⁵⁷ This includes: (i) an inspections management system, with (a) mapping and redesign of inspection planning, execution, and control processes; and (b) development of an integrated inspections management system using artificial intelligence and automated learning mechanisms; (ii) a system for inspecting goods in transit based on risk analysis through: (a) implementation of a central system of virtual inspection in transit; (b) development of an inspection methodology based on risk analysis; and (c) upgrade of the technological and physical infrastructure of inspection units; and (iii) a tax intelligence system, including: (a) mapping and redesign of processes; (b) implementation of an operations monitoring and control system; and (c) implementation of a module for sharing economic/fiscal information with external agencies.
- d. **Implementation of a tax litigation management system**⁵⁸ through: (i) mapping and redesign of processes at SEFAZ/MS and the State of Mato Grosso do Sul Attorney General's Office (PGE/MS); and (ii) solution for automating the tax litigation process, integrated into the corporate systems and available for consultation by taxpayers, with electronic storage of existing processes.
- e. **Implementation of a model for comprehensive services to taxpayers**⁵⁹ through: (i) mapping and standardization of taxpayer service procedures; (ii) introduction of virtual self-help services; (iii) introduction of a system for managing and monitoring taxpayer service processes (services via the Web,

⁵⁵ The virtual agency will provide investors in industry, commerce and services with socioeconomic, environmental and tax information on the State for attracting new businesses.

⁵⁶ [Tax obligations.](#)

⁵⁷ [Inspection and tax intelligence.](#)

⁵⁸ [Tax litigation management.](#)

⁵⁹ [Services to taxpayers.](#)

telephone, or in person), with ongoing evaluation; and (iv) an automated system for managing legislation and smart search tool.

- f. **Implementation of a collection and recovery model⁶⁰** through: (i) mapping and redesign of processes for assessment and collection of tax owed, return of tax payments, and tax claims; (ii) implementation of a collection system that issues management reports; (iii) implementation of a system for return of tax payments; (iv) implementation of a system for managing the assessment of tax owed, available to taxpayers; and (v) implementation of a system for managing tax claims.

1.28 **Component III. Financial administration and public expenditure (US\$8,424,500).** This component seeks to increase the efficiency of financial planning and execution and improve the quality of expenditure. It will finance the following outputs:

- a. **Implementation of a budgetary,⁶¹ financial, accounting, and asset planning and management system.** This includes: (i) identification of a methodology for the strategic forecasting process, priority setting and allocation of resources over the medium term; (ii) preparation of procedural manuals for planning, budget, finance, accounts and assets, respecting the accounting standards applicable to the public sector; (iii) defining a methodology for managing the debt, including fiscal risk analysis; and (iv) introducing an integrated system with modules for planning; budgetary, accounting, financial and asset execution, with accounting conformity and the production of electronic accounts; financial management, with cash flow, control of balances, banking reconciliations, forecasting and monitoring of government transfers, control over accounts payable, management of the public debt, and assets management.
- b. **Implementation of a procurement and contracts management system,⁶²** through: (i) evaluation of procurement macroprocess procedures and consolidation of processes (standardized documents, procurement by sector); (ii) definition of a methodology for managing and enforcing contracts and agreements, integrated into corporate systems; and (iii) a training plan for procurement managers.
- c. **Implementation of a pension management system⁶³** through: (i) development of a single database of pension information; (ii) an integrated pension management system with the following modules: administrative and accounting/financial for the granting of benefits, payslips for retirees and pension recipients, investment portfolio, services, and public input; (iii) development of an intelligence platform; (iv) a census of pension recipients and registry revision; and (v) training in pensions management.

⁶⁰ [Collection and recovery.](#)

⁶¹ [Planning, budgetary, financial, accounting and assets management.](#)

⁶² [Procurement and contract management.](#)

⁶³ [Pension management.](#)

- d. **Implementation of a public expenditure management model**⁶⁴ through: (i) a preinvestment methodology with: (a) definition of the model for managing the public investment cycle; (b) introduction of the preinvestment phase, including procedures, sector studies, support tools, and indicators; (c) review of the legal framework governing investments with public-private partnerships; and (d) implementation of an investment portal; and (ii) a methodology for public cost management with: (a) definition of a conceptual model; (b) implementation of a cost information system; and (c) introduction of a methodology for verifying costs for a given sector.
- 1.29 For all the components, the project will finance consulting services (individual consultants and firms) for US\$4.2 million, nonconsulting services for US\$16.2 million; goods for US\$23.3 million; training for US\$2.5 million; and civil works for US\$5 million, consisting of remodeling of the existing physical premises of SEFAZ/MS units).

C. Key results indicators

- 1.30 **Expected impact and outcomes.** The expected impacts are: (i) a decrease in the ratio of the state's primary fiscal deficit to GDP; (ii) an increase in the ratio of the state's tax revenue intake to GDP; and (iii) a decrease in the ratio of the state's net current debt to GDP. The expected outcomes are: (i) an increase in the ratio of strategic planning goals met to total planned goals; (ii) a decrease in the ratio of cost of tax collection to tax revenue intake; and (iii) a narrowing of the gap between the budget as planned and as executed.
- 1.31 **Economic evaluation.** An [economic analysis](#) of the project looked at the economic/financial costs and benefits, yielding the following conclusions: (i) tax revenues will rise with introduction of a new model for inspection of goods in transit and a new collection model, which will reduce opportunities for evasion and increase the recovery of taxes owed; (ii) taxpayers will benefit from lower costs of compliance with tax obligations, and fewer freight transportation vehicles required to stop at tax inspection posts; and (iii) the state will save resources with the introduction of various process automation and systems integration solutions, especially the payroll management system, the procurement system, and the pensions system. In addition, the integration of systems and redesign of processes will enhance the business climate, with time and cost savings for taxpayers in meeting their tax obligations. At year-end 2027 (10 years), project investments have a net present value of US\$37 million, with an internal rate of return of 50.6%. The results were robust to the sensitivity analysis.

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instruments

- 2.1 **Compliance with the eligibility conditions for the PROFISCO II CCLIP (BR-X1039).** This individual loan operation with the State of Mato Grosso do Sul (MS) is the sixth individual loan operation for specific projects under the PROFISCO II CCLIP (BR-X1039), approved by the Board of Executive Directors pursuant to

⁶⁴ [Public expenditure management](#).

Resolution DE-113/17. The individual loan project meets the eligibility criteria of the CCLIP policy (paragraph 1.21 of document GN-2246-9) and its operational guidelines (document GN-2246-11), given that: (i) the project falls under one of the sectors and components defined under the PROFISCO II CCLIP; (ii) the project is included in the 2018 country program with Brazil;⁶⁵ (iii) the state will implement the operation through the State of Mato Grosso do Sul Department of the Treasury (SEFAZ/MS), which was the same executing agency as for the PROFISCO I – MS individual operation (2327/OC-BR), concluded in October 2016 with 100% of the resources disbursed; and (iv) the findings of the institutional analysis show that the performance level of SEFAZ/MS has not deteriorated, and the same project execution and monitoring tools will be used for this new operation as for the previous one. The project coordination unit (PCU) staff will be the same. The [final progress report for the PROFISCO I – MS individual operation \(2327/OC-BR\)](#) showed that the objectives were satisfactorily achieved, the requirements of the loan contract and the Bank’s disbursement policies were met, and the accounts were audited and presented as required in a timely manner and to an acceptable quality standard.

- 2.2 The project involves an investment loan for specific projects with a total cost of US\$53 million. The Bank will finance US\$47.4 million of that amount (90% of the project cost) from the Ordinary Capital resources, and the local counterpart will be US\$5.3 million (10% of the total project cost), as shown in Table 1.

Table 1. Total budget (US\$)

Categories	IDB	Local	Total	%
A. Direct costs	44,805,700	5,300,000	50,105,700	94.54
Component I. Fiscal management and transparency	23,100,000	3,375,200	26,475,200	49.95
Component II. Tax administration and litigation	15,206,000	-	15,206,000	28.69
Component III. Financial administration and public expenditure	6,499,700	1,924,800	8,424,500	15.90
B. Project management	1,128,800	-	1,128,800	2.13
1. Monitoring	878,800	-	878,800	1.66
2. Evaluation	250,000	-	250,000	0.47
C. Contingencies	1,765,500	-	1,765,500	3.33
Total	47,700,000	5,300,000	53,000,000	100.00
%	90	10	100	

- 2.3 **Disbursement schedule.** Disbursements will be made over a five-year period, as shown in Table 2.

⁶⁵ 2018 Operational Program Report (document GN-2915).

Table 2. Disbursement schedule (US\$)

Source	Year 1	Year 2	Year 3	Year 4	Year 5	Total
IDB	4,221,900	6,876,500	15,740,000	11,813,000	9,048,600	47,700,000
Local	265,000	795,000	1,855,000	1,590,000	795,000	5,300,000
Total	4,486,900	7,671,500	17,595,000	13,403,000	9,843,600	53,000,000
%	8	15	33	25	19	100

B. Environmental and social safeguard risks

2.4 In accordance with the Bank’s Environment and Safeguards Compliance Policy (Operational Policy OP-703), and the results of the safeguard policy filter, the project is classified as category “C.” The project will support the strengthening of taxation and financial processes, with the development of systems and institution-strengthening, so no social or environmental risks are envisaged.

C. Fiduciary risks

2.5 A medium level of fiduciary risk was identified in relation to possible delays in goods and services procurement and contracting processes. This risk will be mitigated through: (i) engagement of individual consultants (specialists and facilitators) to support the technical areas in preparing terms of reference, technical specifications, evaluation criteria, and bidding documents; (ii) creation of a Special Bidding Committee (CEL) devoted exclusively to the PROFISCO II – MS; (iii) definition of the roles, responsibilities, response times, and flow of the State of Mato Grosso do Sul Department of Administration (SAD/MS) procurement process with the internal phases of analysis and approval at SEFAZ/MS and the State of Mato Grosso do Sul Attorney General’s Office (PGE/MS); (iv) implementation of a simplified, fast-tracking process for the PROFISCO II – MS operation with the state treasury; and (v) identification of a focal point at PGE/MS for matters relating to PROFISCO II – MS.

D. Other key risks and issues

2.6 A risk management workshop was held, following the Bank’s methodology, and it was determined that the operation carries medium risk. The risks are as follows:

- a. **Fiscal sustainability (medium risk).** The country may not continue on the sustainable growth path, which could affect the economic and fiscal performance of MS. The main mitigation actions relate to legislation or administrative rules having to do with: (i) [control of public expenditure](#); (ii) increasing the [contribution of civil servants \(active and retired\) to the state social security system](#); (iii) creation of a [Support Fund for the Economic Development and Fiscal Balance of the State of Mato Grosso do Sul \(FADEFE/MS\)](#); ⁶⁶ (iv) adherence to the support plan and stimulus measures to restore fiscal balance offered to the states by the finance ministry

⁶⁶ [FADEFE/MS](#) is constituted by nonmandatory, temporary contributions from firms for the fiscal balance of the state. Its revenue is not of a tax nature, and the PROFISCO II – MS operation will not finance FADEFE/MS activities.

([Supplementary Law 156/2016](#)) through renegotiation and lengthening of the maturities of their debt with the federal government; and (v) [administrative restructuring of the state government](#) to reduce the number of agencies.

- b. **Public management and governance (medium risk).** The state elections in October 2018 may result in a shift of priorities or objectives as new senior officials take over the agencies in charge of the project. This risk will be mitigated by assigning permanent technical staff of the state to the PCU, and entering into a management contract with the departments involved in project execution, to establish communication immediately with the new government team.
 - c. **Development (medium and high risk).** The following risks were rated as medium: (i) delays in the delivery of outputs under the responsibility of the state agencies involved in the project execution; this risk will be mitigated through the signature of cooperation agreements between SEFAZ/MS and SEGOV/MS, SAD/MS, CGE/MS, and PGE/MS, designating focal points at the PCU; and (ii) management and compliance monitoring of contracts lacking in support tools or a technical team to validate outputs; this risk will be mitigated through the priority contracting of a contract management and compliance monitoring methodology and the respective management system. The following risks were rated as high: delays in the development of project processes and systems due to the limited responsiveness of the SEFAZ/MS IT area in defining the technical requirements. This risk will be mitigated through the technical audit of IT solutions, especially the planning and finance system and the public procurement system; the automation of state processes; and the appointment of an IT specialist to the PCU team.
- 2.7 **Program sustainability.** In addition to the measures already being taken by the government (see paragraph 2.6.a), the project includes measures that will foster fiscal sustainability in the medium and long term, such as reduced expenditure and tax evasion, which will result in greater revenues. To guarantee that the capacity-building from the project is sustainable after execution ends, PROFISCO II – MS includes actions to reduce personnel expenditure and cut procurement and service delivery costs, as well as raise revenues through improved tax enforcement and recovery of tax claims. The related outputs include: payroll management integrated into the planning and finance system; pension management, unification of tax rolls and simplification of tax obligations; management of tax concessions; use of new technologies for tax compliance and tax intelligence (see "[Economic analysis](#)"). For investments in information and communication technologies (ICT), SEFAZ/MS will mainly use its own personnel, supported by consultants, for in-house development. The project will also finance the ICT and Information Security Master Plan, which specifies responsibilities and resources for maintaining and updating the IT infrastructure.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

- 3.1 The borrower is the State of Mato Grosso do Sul (MS),⁶⁷ which will execute the operation through its Department of the Treasury (SEFAZ/MS). The Federative Republic of Brazil will be the guarantor of the borrower's financial obligations, in accordance with the policy on guarantees required from borrowers (document GP-104-2). A project coordination unit (PCU) will be established for project execution. The PCU will have a coordinator, a procurement specialist, an ICT specialist, an administrative/financial specialist, and a planning and monitoring specialist. The PCU will coordinate the activities related to monitoring, evaluation, and auditing, in order to monitor that the project is executed properly, and its objectives met.
- 3.2 The main functions of the PCU will include: (i) planning the execution of activities; (ii) implementing and updating the project's operational tools: [project execution plan](#), [annual work plan](#), and [procurement plan](#); (iii) supervising execution and submitting status reports; (iv) conducting the processes for the preparation of terms of reference, procurement of goods, and selection and contracting of services; (v) submitting supporting documentation and disbursement requests to the Bank; (vi) preparing financial statements; and (vii) delivering the project evaluation. The borrower will comply with the program [Operating Regulations](#) approved by the Bank for the PROFISCO II CCLIP, which establish: (i) eligibility criteria for projects and outputs eligible for financing; (ii) project execution roles, procedures, and rules; and (iii) operational and contractual relationships between the parties involved in the project.
- 3.3 **Coordination mechanism.** SEFAZ/MS will cooperate with the State of Mato Grosso do Sul Attorney General's Office (PGE/MS), Department of the Interior and Strategic Management (SEGOV/MS), Department of Administration (SAD/MS), and Comptroller General's Office (CGE/MS) for execution of the activities benefiting them. Leaders will be appointed for the corresponding outputs at those institutions, who will coordinate their actions with the PCU and supervise their technical development and implementation. For the coordination of these activities related to public governance, public oversight and transparency, tax litigation, procurement and public expenditure, payroll management and pension expenditure, and primarily for their respective procurements, information flows and processes will be mapped and defined among the beneficiaries, the PCU, and the Special Bidding Committee (CEL), clarifying roles, responsibilities and time frames that will be built into the institutional structure through cooperation instruments (see paragraph 3.5).
- 3.4 **Special contractual conditions precedent to the first disbursement of the loan proceeds:** (i) the borrower will adhere to the program [Operating Regulations](#) previously approved by the Bank for all individual operations under the PROFISCO II CCLIP; and (ii) the project coordination unit (PCU) will be

⁶⁷ The analysis of the [financial condition of the state of MS](#) confirms its payment capacity to meet the debt service obligations undertaken with this loan, which represents 0.015% of state GDP and 0.14% of net current revenues in 2016. In addition, the state is meeting the requirements of the Fiscal Responsibility Law and the conditions of the [MS Fiscal Adjustment and Restructuring Program](#).

- established, and its members appointed.** These conditions are essential for guaranteeing that the executing agency has detailed regulations covering operational and fiduciary aspects, and for mitigating the risks of delay in project execution. This practice was adopted in PROFISCO I and proved to be successful in allowing the coordination and guidance issues relevant to the executing agencies to be consolidated into the program Operating Regulations and ensuring that the responsibilities of the PCU members were distributed more efficiently according to technical area, financial area, procurement, and monitoring and planning.⁶⁸
- 3.5 **Special contractual condition for execution.** Prior to the start of activities whose beneficiaries will be the State of Mato Grosso do Sul Department of the Interior and Strategic Management (SEGOV/MS), Department of Administration (SAD/MS), Comptroller General's Office (CGE/MS), and Attorney General's Office (PGE/MS), the executing agency will sign cooperation agreements with those entities to establish the roles and responsibilities of the parties as part of program execution. The activities will be coordinated with: (i) SEGOV/MS: public governance, under Component I, and quality of public management, under Component III; (ii) CGE/MS: public control and transparency, under Component I; (iii) SAD/MS: payroll management, under Component I, and procurement management and pension expenditure, under Component III; and (iv) PGE/MS: tax litigation, under Component II. This condition was adopted with success in PROFISCO I and allowed specific responsibilities to be identified by entity, considering the implementation of the planned outputs under the components. Adopting this practice again is justified to guarantee the mechanism for coordination among these entities, which are independent of SEFAZ/MS, and to mitigate the risk of outputs being delayed during execution (see paragraph 2.6.c).
- 3.6 **Procurement.** Project procurement and contracting will comply with the Policies for the Procurement of Goods and Works Financed by the IDB (document GN-2349-9) and Policies for the Selection and Contracting of Consulting Services Financed by the IDB (document GN-2350-9), together with the provisions of the [procurement plan](#).
- 3.7 **Single-source selection.**⁶⁹ Under condition 3.10(d) of the Policies for the Selection and Contracting of Consulting Services Financed by the IDB (document GN-2350-9), "when only one firm is qualified or has experience of exceptional worth for the assignment," the following will be engaged via single-source selection: (i) training schools, data processing companies, universities, and government research centers (eligible under paragraph 1.11(c) of the policies), which have extensive experience and adequate infrastructure to train public officials and provide technical assistance, chiefly in the use of new IT solutions;⁷⁰

⁶⁸ [Report on PROFISCO I PCUs, 2015](#).

⁶⁹ For more detail, see Annex III, Chapter V.

⁷⁰ These entities are: (i) Escola de Administração Fazendária [School of Finance Administration] (ESAF); (ii) Escola Nacional de Administração Pública [National School of Public Administration] (ENAP) of the Ministry of Planning, Development, and Management (MPDG); (iii) schools of the state government; (iv) data processing companies; (v) federal and state universities; (vi) Instituto de Pesquisa Econômica Aplicada [Institute of Applied Economic Research] (IPEA); and (vii) Instituto de Estudos Fiscais [Institute of Fiscal Studies] (IEF).

and (ii) the Inter-American Center of Tax Administrations (CIAT), an international agency, given its specialization in technical assistance for the modernization of tax administrations in the region.

- 3.8 **Audited financial reports.** The borrower will deliver audited financial reports to the Bank annually within 120 days after the close of each fiscal year of SEFAZ/MS. The external audit will be performed by an external audit firm acceptable to the Bank, or by the State of Mato Grosso do Sul Audit Office (TCE/MS).⁷¹ SEFAZ/MS will contract the audits for the entire project using terms of reference will require the Bank's no objection.

B. Summary of arrangements for monitoring results

- 3.9 **Monitoring.** Monitoring will be based on: (i) [the PEP and the AWP](#), (ii) the procurement plan, (iii) the Results Matrix, (iv) the [monitoring and evaluation plan \(MEP\)](#), and (v) the progress monitoring report (PMR). The PCU will prepare six-monthly reports on progress toward the outcome, output, and financial targets for the Bank's approval. The Bank will conduct inspection visits and ex post reviews as part of project monitoring.
- 3.10 **Evaluation.** The project will be evaluated against the annual targets and indicators for impacts and outcomes in the project's Results Matrix, through a before-and-after comparison of results. The MEP calls for an independent midterm evaluation, 90 days after the close of the third year of project execution, and a final evaluation, 90 days after 95% of the loan proceeds have been disbursed. The evaluation reports will serve as input for the program completion report for the PROFISCO II CCLIP.

⁷¹ TCE/MS and the Bank have signed a [memorandum of understanding](#) for audits of loan and technical cooperation contracts in the state.

Development Effectiveness Matrix		
Summary		
I. Corporate and Country Priorities		
1. IDB Development Objectives	Yes	
Development Challenges & Cross-cutting Themes	-Productivity and Innovation -Institutional Capacity and the Rule of Law	
Country Development Results Indicators	-Percent of GDP collected in taxes (%) -Government agencies benefited by projects that strengthen technological and managerial tools to improve public service delivery (#)* -Subnational governments benefited by decentralization, fiscal management and institutional capacity projects (#)* -Accountability institutions strengthened (#)*	
2. Country Development Objectives	Yes	
Country Strategy Results Matrix	GN-2850	Promote the improvement of the business climate and improve efficiency in the management of public resources.
Country Program Results Matrix	GN-2915	The intervention is included in the 2018 Operational Program.
Relevance of this project to country development challenges (If not aligned to country strategy or country program)		
II. Development Outcomes - Evaluability		
3. Evidence-based Assessment & Solution	Evaluable	
3.1 Program Diagnosis	9.6	
3.2 Proposed Interventions or Solutions	3.0	
3.3 Results Matrix Quality	3.6	
4. Ex ante Economic Analysis	3.0	
4.1 Program has an ERR/NPV, or key outcomes identified for CEA	9.0	
4.2 Identified and Quantified Benefits and Costs	3.0	
4.3 Reasonable Assumptions	3.0	
4.4 Sensitivity Analysis	1.0	
4.5 Consistency with results matrix	2.0	
5. Monitoring and Evaluation	0.0	
5.1 Monitoring Mechanisms	8.0	
5.2 Evaluation Plan	2.5	
5.2 Evaluation Plan	5.5	
III. Risks & Mitigation Monitoring Matrix		
Overall risks rate = magnitude of risks*likelihood	Medium	
Identified risks have been rated for magnitude and likelihood	Yes	
Mitigation measures have been identified for major risks	Yes	
Mitigation measures have indicators for tracking their implementation	Yes	
Environmental & social risk classification	C	
IV. IDB's Role - Additionality		
The project relies on the use of country systems		
Fiduciary (VPC/FMP Criteria)	Yes	Financial Management: Budget, Treasury, Accounting and Reporting, External Control, Internal Audit. Procurement: Information System, Comparison.
Non-Fiduciary	Yes	Strategic Planning National System, Statistics National System.
The IDB's involvement promotes additional improvements of the intended beneficiaries and/or public sector entity in the following dimensions:		
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project	Yes	

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

Evaluability Assessment Note:

The main goal of the operation is to contribute to the fiscal sustainability of the State of Mato Grosso Do Sul. To achieve this end, the proposal defines three specific areas on which the project will intervene. The first area is fiscal management and transparency. The second area is tax administration and litigation. The third area is financial administration of public expenditure. Each of these areas define a component. The document includes a description of the process gaps that lead to weaknesses in each of these three areas. The project is the child of a series of operations under the Conditional Credit Line for Investment Projects (CCLIP) parent BX-L1502.

The project proposal diagnoses a primary balance as a share of the State PIB of 0.04 percent in 2016, and a Current Net Debt as a share of the State PIB of 7.49 Percent (SEFAZ, 2016). The diagnosis is based on the MD-GEFIS tool which analyzes processes in the three main areas which define the components. The Ministry of Finance provides a diagnosis for a total of seventeen sub areas. Each diagnosis identified the main restrictions for the Ministry to increase tax revenue, decrease running costs or improve efficiency in expenditures, and improve service delivery to citizens. Overall, the diagnosis identifies gaps in institutional arrangements (such as weak coordination and outdated legal documents), deficits in personnel management and training, and gaps in capital investments (resulting in outdated technological infrastructure, limited availability of information, and lack of mechanisms to communicate with citizens). The quantification of these needs is disaggregated for 16 processes.

The economic analysis provides a quantification of efficiency gains to government services and savings to taxpayers. Efficiency gains are derived from seven areas which include savings by better control of payroll, reductions in cost to monitor merchandises in transit, and reductions in costs derived from an improved shopping system. The costs include investment in technology and maintenance. The analysis concludes with a net present value of about US\$17 million.

Monitoring relies on reports by multiple government agencies with a majority of indicators provided by the Ministry of Finance. The ex post evaluation plan includes a before-after comparison and an ex-post economic analysis. The project also proposes a synthetic cohorts approach to evaluate the effects of the program on results indicators. However, the methodology proposed is not appropriate to identify program effects.

There is only one risk out of six classified as high. The main risk identified for the program to succeed are delays in the development of processes and systems. These delays could result from a weak capacity by the information technology department. The mitigation measures include an independent contract to evaluate scenarios, the ex-ante definition of processes, and the designation of an IT specialist in the executing unit.

RESULTS MATRIX

Project objective:	The project objective is to contribute to the state's fiscal sustainability through: (i) modernization of fiscal management; (ii) improvement of tax administration; and (iii) improvement of public expenditure management.
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EXPECTED IMPACT

Indicators	Unit of measure	Baseline	Base year	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
Impact 1: Decrease in the state's primary fiscal deficit/GDP ratio											
Primary balance / GDP-MS	%	-1.60	2017	0.02	0.05	0.07	0.08	0.10	0.10	Budget Execution Report, SEFAZ/MS	See MEP
Impact 2: Increase in the state's tax revenue/GDP ratio											
Tax revenue / GDP-MS	%	10.16	2017	10.26	10.35	10.44	10.53	10.61	10.61	Tax Administration Report, SEFAZ/MS	See MEP
Impact 3: Decrease in state's net current debt/GDP ratio											
Net current debt / GDP-MS	%	7.96	2017	7.88	7.80	7.69	7.56	7.56	7.56	Treasury Report, SEFAZ/MS	See MEP

EXPECTED OUTCOMES¹

Outcome indicators	Unit of measure	Baseline	Year baseline	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Target year	Means of verification	Comments
Outcome 1: Increase in the ratio of strategic planning targets met to total planned targets												
Number of targets met / Total planned targets	%	66.4	2017	72.4	74.5	76.9	79.5	82.3	82.3	2023	Management Contract Evaluation Report, SEGOV/MS	See MEP
Outcome 2: Decrease in the ratio of cost of tax collection to tax revenue intake												
SEFAZ operating budget / Tax revenue intake	%	4.12	2017	4.05	4.0	3.97	3.94	3.90	3.90	2023	Financial Report, SEFAZ/MS State balance sheet	See MEP
Outcome 3: Narrowing of the gap between the budget as planned and as executed												
Budget as planned / Budget as executed	%	-3.55	2017	11.5	11.0	10.5	10.0	9.5	9.5	2023	State balance sheet	See MEP

¹ The expected outcomes are cumulative.

OUTPUTS²

Outputs	Unit of measure	Baseline	Year baseline	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
Component 1: Fiscal management and transparency											
1.1 Public governance model ³ implemented	Model	0	2017	0	0	0	0	1	1	Management Report, SEGOV/MS	See MEP
1.2 State comptroller model implemented	Model	0	2017	0	0	0	0	1	1	Management Report, CGE/MS	See MEP
1.3 Model for skills-based personnel management implemented	Model	0	2017	0	0	0	0	1	1	Human Resources Management Report, SEFAZ/MS	See MEP
1.4 Software system ⁴ for payroll management implemented	Software	0	2017	0	0	0	0	1	1	Treasury Report-SEFAZ/MS	See MEP
1.5 ICT management and operations model implemented	Model	0	2017	0	0	0	0	1	1	ICT Management Report, SEFAZ/MS	See MEP
1.6 Web-based platform for transparency and fiscal citizenship implemented	Web-based platform	0	2017	0	0	0	0	1	1	Access to website and PCU status report	See MEP

² The results are annual.

³ Model includes: (i) procedures and business rules defining its functioning; (ii) software application or IT system supporting its operationalization; (iii) training in software operation and procedures; and (iv) in many cases, the necessary expansion in processing capacity with more servers, user PCs, storage devices (given the increase in data volumes), and improved communications for remote users.

⁴ The software application or IT system implementing a set of rules to support the operationalization of the conceptual business model.

Outputs	Unit of measure	Baseline	Year baseline	Year 1	Year 2	Year 3	Year 4	Year 5	Final target	Means of verification	Comments
Component 2: Tax administration and litigation											
2.1 Software system for managing tax concessions implemented	Software	0	2017	0	0	0	0	1	1	SEFAZ/MS Tax Action Management Report	See MEP
2.2 Simplified software systems for tax obligations (mandatory outputs)	Software	0	2017	0	0	1	1	1	3	SEFAZ/MS Tax Action Management Report	See MEP
2.3 Software systems for inspection and tax intelligence implemented	Software	0	2017	0	0	0	1	2	3	SEFAZ/MS Tax Action Management Report	See MEP
2.4 Software systems for tax litigation management implemented	Software	0	2017	0	0	1	0	0	1	Tax Litigation Management Report, SEFAZ/MS	See MEP
2.5 Model for comprehensive services to taxpayers implemented	Model	0	2017	0	0	0	0	1	1	Management Report, SEFAZ/MS	See MEP
2.6 Collection and recovery model implemented	Model	0	2017	0	0	0	0	1	1	Compliance report from the PGE/MS	See MEP
Component 3: Financial administration and public expenditure											
3.1 Software system for budgetary, financial, accounting and asset planning and management (SIAFI) implemented	Software	0	2017	0	0	0	0	1	1	SEFAZ/MS Financial Report	See MEP
3.2 Software system for procurement and contracts management implemented	Software	0	2017	0	0	0	0	1	1	SEFAZ/MS Treasury Report	See MEP
3.3 Software system for pension management implemented	Software	0	2017	0	0	0	0	1	1	Management Report, SAD/MS	See MEP
3.4 Public expenditure quality management model implemented	Model	0	2017	0	0	0	0	1	1	Management Report, SEGOV/MS	See MEP

FIDUCIARY AGREEMENTS AND REQUIREMENTS

Country:	Federative Republic of Brazil
Project number:	BR-L1511
Name:	Fiscal Management Modernization Project for the State of Mato Grosso do Sul – PROFISCO II – MS
Executing agency:	State of Mato Grosso do Sul, acting through its Department of the Treasury (SEFAZ/MS)
Fiduciary team:	Fábia Assis Bueno and Marília Santos (VPC/FMP)

I. EXECUTIVE SUMMARY

- 1.1 The institutional evaluation for the project's fiduciary management was based on: (i) the country's current fiduciary context; (ii) the findings of the assessment of principal fiduciary risks; (iii) the MD-GEFIS report; (iv) the institutional analysis; (v) prior experience under PROFISCO I; and (vi) working meetings with the Project Team and SEFAZ/MS.
- 1.2 Brazil has robust country fiduciary systems that enable sound management of administrative, financial, oversight, and procurement processes, in accordance with the principles of transparency, economy, and efficiency. The executing agency's systems related to its planning and organization, execution, and control capacity have a medium level of development and represent a medium risk.
- 1.3 SEFAZ/MS has the legal capacity and experience to execute the project activities, considering that this is PROFISCO's second phase. The structure implemented and strengthened will be utilized, drawing on lessons learned from execution of the first phase.

II. FIDUCIARY CONTEXT OF THE EXECUTIVE AGENCY

- 2.1 The structure of SEFAZ/MS consists of (i) the Superintendencies of Tax Administration, Treasury, Information Management, General Accounting, Budget, Administration and Finance, Logistics and Infrastructure; and (ii) support, coordination, and advisory bodies, including the Coordination Office of the Special Unit for the Modernization of State Administration (CONEMAE).
- 2.2 Project activities will be executed by SEFAZ/MS through its program coordination unit (PCU), which is responsible for institutional and technical coordination within CONEMAE.
- 2.3 The project will benefit the executing agency and the following agencies: the State of Mato Grosso do Sul Department of the Interior and Strategic Management (SEGOV/MS), Department of Administration (SAD/MS), Comptroller General's Office (CGE/MS), and Attorney General's Office (PGE/MS).

- 2.4 Procurement policy is the responsibility of the Superintendency of Competitive Bidding within SAD/MS, which will conduct all procurement processes under the program.
- 2.5 The executing agency is subject to internal control by CGE/MS through its coordination offices for internal control, and external control is exercised by the State of Mato Grosso do Sul Audit Office (TCE/MS).

III. INSTITUTIONAL CAPACITY ASSESSMENT, FIDUCIARY RISK, AND MITIGATION MEASURES

- 3.1 The institutional capacity assessment and its validation with staff of SEFAZ/MS, SEGOV/MS, SAD/MS, CGE/MS, and PGE/MS concluded that the executing agency has a medium level of institutional capacity with experience in the execution of operations with the Bank.
- 3.2 TCE/MS and the Bank have signed a memorandum of understanding for audits of loan and technical cooperation contracts in the state. The project will provide resources for the training of auditors.
- 3.3 A medium level of fiduciary risk was identified in relation to possible delays in goods and services procurement and contracting processes. This risk will be mitigated through: (i) engagement of individual consultants (specialists and facilitators) to support the technical areas in preparing terms of reference, technical specifications, evaluation criteria, and bidding documents; (ii) creation of a Special Bidding Committee (CEL) devoted exclusively to the PROFISCO II – MS; (iii) definition of the roles, responsibilities, response times, and flow of the State of Mato Grosso do Sul Department of Administration (SAD/MS) procurement process with the internal phases of analysis and approval at SEFAZ/MS and the State of Mato Grosso do Sul Attorney General's Office (PGE/MS); (iv) implementation of a simplified, fast-tracking process for the PROFISCO II – MS operation with the state treasury; and (v) identification of a focal point at PGE/MS for matters relating to PROFISCO II – MS.

IV. CONSIDERATIONS FOR THE SPECIAL PROVISIONS OF THE LOAN CONTRACT

- 4.1 **Special contractual condition precedent to first disbursement of the loan proceeds. SEFAZ/MS will provide evidence that the Special Bidding Committee (CEL) has been established.** This condition is justified in order to avoid delays and ensure that procurement processes are conducted as scheduled. This recommendation is based on the satisfactory experience of the PROFISCO I project PCUs, which fast-tracked the proposed bidding documents and had a team dealing specifically with the relevant Bank policies.¹

¹ [Report on PROFISCO I PCUs, 2015.](#)

V. AGREEMENTS AND REQUIREMENTS FOR PROCUREMENT EXECUTION

5.1 The fiduciary agreements for procurement establish the provisions applicable to execution of all planned procurements for the project.

A. Procurement execution

5.2 **Procurement of works, goods, and nonconsulting services.** The contracts will be subject to international competitive bidding (ICB) and will be executed using the standard bidding documents (SBDs) issued by the Bank. Bidding processes subject to national competitive bidding (NCB) will be executed using the country bidding documents agreed upon with the Bank.

5.3 **Selection and contracting of consultants.** The contracts will be executed using the standard request for proposals (RFP) issued by the Bank. The sector specialist will be responsible for reviewing terms of reference for the contracting of consulting services. Consultants will be selected and contracted in accordance with the Policies for the Selection and Contracting of Consultants Financed by the Inter-American Development Bank (document GN-2350-9).

5.4 **Use of country procurement system.** The *Pregão Eletrônico* electronic reverse auction system, which is the country procurement (sub)system approved by the Bank, will be used for the procurement of off-the-shelf goods up to an amount of US\$5 million. Any system or subsystem subsequently approved will be applicable to the operation. The procurement plan and its updates will state which procurement processes will be executed using the approved country systems.

5.5 **Advance procurement / retroactive financing.** No advance procurement or retroactive financing is envisaged.

B. Single-source selection

5.6 Under the condition of the Policies for the Selection and Contracting of Consulting Services Financed by the IDB (document GN-2350-9), "when only one firm is qualified or has experience of exceptional worth for the assignment," the following will be engaged via single-source selection:

5.7 **Schools and government agencies.** Given the way treasury and finance departments are organized in Brazil, outside entities are responsible for knowledge and skills development: (i) Escola de Administração Fazendária [School of Finance Administration] (ESAF); (ii) Escola Nacional de Administração Pública [National School of Public Administration] (ENAP) of the Ministry of Planning, Development, and Management (MPDG); (iii) government schools for the training of public officials; (iv) data processing companies, responsible for IT development in the states; and (v) federal and state universities that provide technical assistance for new IT solutions. To ensure the sustainability of the outputs developed and financed by the project, single-source selection will be used to engage federal and state entities devoted to the training of public officials and IT development, under paragraphs 1.11.c and 3.10 of document GN-2350-9.

5.8 **Specialized international agencies.** The Inter-American Center of Tax Administrations (CIAT), an international agency, will also be engaged under paragraphs 3.10 and 3.15 of document GN-2350-9, given its specialization in technical assistance for the modernization of tax administrations.

- 5.9 **Research and study institutes.** Instituto de Pesquisa Econômica Aplicada [Institute of Applied Economic Research] (IPEA) and Instituto de Estudos Fiscais [Institute of Fiscal Studies] (IEF) will be engaged under paragraph 3.10.d of document GN-2350-9. IPEA is Brazil’s leading research center in Brazil with an international reputation in the production of scientific data and studies. IEF is part of Spain’s Ministry of Finance and Public Administration and promotes training activities for civil servants to improve their skills for the performance of their duties.

Table 1. Thresholds for ICB and international short list

Method	ICB Works	ICB Goods and nonconsulting services	International short list for consulting services
Threshold	US\$25 million	US\$5 million	US\$1 million

Table 2. Main procurements

Contract purpose	Selection method	Estimated date	Estimated amount (US\$ million)
Goods and nonconsulting services			
Purchase of “safe room”	Country system	Q3/2019	4.85
Purchase of servers, storage, and related software	Country system	Q1/2019	4.70
Implementation of Planning and Finance System (SPF)	Country system	Q4/2019	4.01

* Click [here](#) to access the 18-month procurement plan.

C. Procurement supervision

- 5.10 The supervision method will be ex post, except where ex ante supervision, and single-source selection, is justified. When the country system is used for procurement, the country system will also be used for supervision.
- 5.11 The supervision method must be identified for each selection process. Ex post reviews will be conducted every twelve months in accordance with the project supervision plan. The ex post review reports will include at least one physical inspection visit, selected from among the procurement processes subject to ex post review.

Table 3. Threshold for ex post review

Works	Goods	Consulting services
NCB and Shopping	NCP and <i>Pregão Eletrônico</i>	Less than US\$1 million

D. Records and files

- 5.12 The PCU will be responsible for process documentation and will retain the necessary documentation for supervision and auditing purposes.

VI. FINANCIAL MANAGEMENT

- 6.1 **Programming and budget.** SEFAZ/MS, acting through the PCU, will coordinate with SEGOV/MS on the entire process of planning for the execution of activities as set out in the project execution plan (PEP) and in the annual work plan (AWP). State entities use the following planning instruments: Multiyear Plan (PPA), Budgetary Guidelines Law (LDO), which lays down budget directives, and Annual Budget Law (LOA). The project budget will form part of the LOA.
- 6.2 The PCU will ensure that the budgetary resources for the project, Bank, and local contribution are budgeted annually and earmarked for execution in accordance with the project schedule. Budgetary resources must be recorded in the year of execution in the Sistema de Planejamento e Finanças [Planning and Finance System] (SPF) as an external source. The LOA must include the funds necessary for implementation, including both the external loan and the local counterpart.
- 6.3 **Accounting and information systems.** In Mato Grosso do Sul, public entities work with the SPF, which was used in PROFISCO I. The SPF performs all financial, accounting, and financial planning execution for state operations. The SPF is not integrated with other corporate systems. In PROFISCO I, MS-Access was used to issue project disbursements, audited financial reports, and statements.
- 6.4 The state is in the process of converting to International Accounting Standards, which will entail the preparation of financial manuals and review of workflows.
- 6.5 **Disbursements and cash flow.** The project will use the country cash management system of the state. Expenditures will be subject to the budgetary and financial implementation processes and duly recorded in the SPF system.
- 6.6 As under PROFISCO I, the Bank resources will be administered through an exclusive account so that the loan proceeds can be identified and reconciled. This includes deposits and payments.
- 6.7 Disbursements will be made in U.S. dollars under the advance of funds modality. Advances will be based on a projection of financial resources for up to 120 days. Future advances will require accounting for at least 80% of the cumulative total amount for which supporting documentation has not been provided.
- 6.8 Expenses deemed ineligible by the Bank must be repaid from local contribution resources or other resources, at the Bank's discretion, depending on the nature of the ineligibility.
- 6.9 The exchange rate agreed upon with the executing agency for the purpose of accounting for expenditures paid with resources from the advances of funds under the loan will be the "internalization rate." To determine the equivalency of expenditures incurred from the local counterpart or the reimbursement of expenditures chargeable against the loan, the agreed exchange rate will be the rate on the date the expenditure is paid.
- 6.10 **Internal control and internal audit.** The state's internal control is exercised by the State of Mato Grosso do Sul Comptroller General's Office (CGE/MS), which is the hub of the internal control system of the executive branch. CGE/MS was established in 2016, and performs the functions of internal control, government audit, public

- hearings, public transparency, and societal oversight. Project activities will come under its control.
- 6.11 **External control and reports.** External control is exercised by the State of Mato Grosso do Sul Audit Office (TCE/MS). The external audit of PROFISCO II will be performed by TCE/MS or a firm of external auditors eligible for the Bank.
- 6.12 The audited financial reports will be delivered, in accordance with terms of reference agreed with the Bank, by TCE/MS or a firm of external auditors eligible for the Bank, within 120 days after the close of each fiscal year.
- 6.13 **Financial supervision plan.** This plan may be amended during execution to reflect changes in risk levels or the need for additional oversight.

Table 4. Supervision plan

Nature and scope	Frequency	Responsibility	
		Bank	Executing agency
Ex post review of disbursements and procurement	Annual	Fiduciary team	PCU – External Auditor – TCE/MS
Annual audit	Annual	Fiduciary team	PCU – External Auditor – TCE/MS
Review of disbursement requests	Periodic	Fiduciary team	
Supervision visit	Annual	Fiduciary specialist	

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

RESOLUTION DE-___/18

Brazil. Loan ___/OC-BR to the State of Mato Grosso do Sul. Fiscal Management Enhancement Project for the State of Mato Grosso do Sul – PROFISCO II - MS Sixth Individual Loan Operation under the Conditional Credit Line for Investment Projects (CCLIP) BR-X1039 – Fiscal Management Modernization Program in Brazil – PROFISCO II

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the State of Mato Grosso do Sul, as Borrower, and with the Federative Republic of Brazil, as Guarantor, for the purpose of granting the former a financing aimed at cooperating in the execution of the Fiscal Management Enhancement Project for the State of Mato Grosso do Sul - PROFISCO II - MS, which constitutes the sixth individual loan operation under the Conditional Credit Line for Investment Projects (CCLIP) BR-X1039 - Fiscal Management Modernization Program in Brazil – PROFISCO II, approved on 8 December 2017 by Resolution DE-113/17. Such financing will be for the amount of up to US\$47,700,000, from the resources of the Bank's Ordinary Capital, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on _____ 2018)

LEG/SGO/CSC/EZSHARE-620307903-33926
Pipeline: BR-L1511