International Monetary Fund

Bolivia and the IMF

Press Release:
IMF Executive Board Completes Fifth Review Under Bolivia's Stand-By Arrangement, Approves US$14.5 million Disbursement, a US$64.5 Augmentation and an Extension of The Arrangement
April 8, 2005

Country's Policy Intentions Documents

E-Mail Notification
Subscribe or Modify your subscription

Bolivia: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

March 24, 2005

The following item is a Letter of Intent of the government of Bolivia, which describes the policies that Bolivia intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Bolivia, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.

La Paz, Bolivia, March 24, 2005

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. de Rato,

1. The macroeconomic policies and structural reforms pursued by our government continue to bear fruit despite difficult political and social conditions. Macroeconomic developments in 2004 were positive with real GDP growth of nearly 4 percent, a significant current account surplus, and increased reserve coverage of deposits.

2. Our program, supported under a Stand-By Arrangement (SBA), was broadly on track in 2004. The quantitative performance criteria (PCs) for end-September were met, except for that on central bank net credit to the nonfinancial public sector (NFPS), which was missed by a marginal amount (less than US$1.5 million). By end-December, central bank credit was back on track and the deficit target was met with a margin. Thus, we are requesting a waiver for the nonobservance of the end-September PC on central bank net credit to the NFPS. We are also requesting a waiver for the nonobservance of the end-September structural PC on congressional approval of the procedural requirements for appeals before the Tax Superintendency. While compliance with this PC was outside the control of the government, we are already working to broaden consensus for the reform agenda with congressional representatives.

3. In support of our policies described in the attached Memorandum of Economic and Financial Policies (MEFP), the Government of Bolivia requests the completion of the fifth review under the SBA, and an extension of the SBA through March 31, 2006, with an increased access level in an amount equivalent to SDR 42.86 million (25 percent of quota). We also request that the remaining amounts available under the Stand-by Arrangement, as well as the amounts corresponding to the requested increased access, be rephased over the next 12-months in four purchases linked to current and subsequent reviews. We finally ask for the establishment of the quantitative PCs for end-June, end September, and end-December 2005 specified in table 1 of the MEFP; and of the structural PCs specified in Table 3 of the MEFP. Performance under the program will be assessed at the sixth, seventh, and eight reviews to be completed by mid-August 2005, mid-November 2005 and mid-February 2006, respectively.

4. We implemented the prior actions specified in Table 3 of the MEFP before the above-requests were considered by the IMF Board.

5. The Government believes that the policies set forth in the attached MEFP are adequate to achieve the objectives of its program, but will take any further measures that may become appropriate for this purpose. Bolivia will consult with the Fund on the adoption of these measures and in advance of revisions to the policies contained in the MEFP, in accordance with the Fund's policies on such consultation.

Sincerely yours,

_______/s/________	____________/s/______________
Luis Carlos Jemio	Juan Antonio Morales
Minister of Finance	President, Central Bank of Bolivia

Supplementary Memorandum of Economic and Financial Policies of the Government of Bolivia
Fifth Review under the Stand-By Arrangement, Request for Waiver of Nonobservance of Performance Criteria, Rephasing, Augmentation and Extension of the Stand-By Arrangement

March 24, 2005

1. Despite difficult social and political conditions, we continue to implement a solid macroeconomic program, while gradually reducing social tensions. We have observed all end-September quantitative PCs, except that on central bank net credit to the nonfinancial public sector, which was missed by a marginal amount (less than US$1.5 million). Based on preliminary data, we met all the indicative quantitative targets for end-2004, some with wide margins, except the net domestic financing target, as external disbursements were lower than expected. The recommendations of the expenditure commission were published in September (structural PC). Unfortunately, the more protracted and difficult discussions on the hydrocarbons bill have not allowed us to yet adopt a strategy on gas exports as intended (structural benchmark).

2. The program will continue to be guided by the macroeconomic and structural reform policies described in the Memorandum of March 21, 2003, and modified by the Supplementary Memoranda of June 20, 2003, September 24, 2003, June 2, 2004, September 20, 2004 and December 16, 2004.

3. The next review under the proposed extension of the SBA would focus on assessing progress toward (i) a draft 2006 budget and tax reform package, consistent with a deficit close to 4 percent of GDP, and subject to the availability of concessional financing; (ii) the adoption of a gas exports strategy, including securing Congressional approval of a hydrocarbons bill consistent with increased investment and exports; and (iii) reducing financial vulnerabilities, including those arising from high indebtedness. The test date for quantitative PCs to be assessed at the sixth review would be end-June 2005.

A. Macroeconomic Framework

4. Stronger than expected exports—particularly hydrocarbons—have driven economic activity, with real GDP growth estimated at 3¾ percent in 2004 in line with the program. 12-month inflation was 4.6 percent by end-year, exceeding the program target of 3½ percent, owing mainly to imported inflation. The external current account surplus is estimated to have been around 3 percent of GDP in 2004, with strong growth in gas, minerals, and agricultural exports.

B. Fiscal Policy

5. Preliminary estimates for 2004 point to a deficit of 5.7 percent of GDP, 0.3 percentage points of GDP below the indicative target. Tax revenues were 1.0 percent of

GDP higher than programmed, largely due to stronger than expected collection from the tax amnesty and hydrocarbons exports. With higher revenues, we were able to accelerate the implementation of high-priority road and other pro-growth projects, leading to higher than programmed investment by 0.6 percent of GDP. Pro-poor spending is estimated to have increased by 0.2 percent of GDP. Reflecting our austerity efforts, current expenditures have been contained in line with the program.

6. The 2005 budget submitted by the Executive in September 2004 acquired legal status in December, after Congress did not formally approve it within the period established by the Constitution. The budget, combined with a balanced fiscal package already adopted through supreme decrees and ministerial resolutions, is consistent with a deficit target of 5¼ percent of GDP and a maximum net use of nonconcessional financing of 1½ percent of GDP. We would aim at a lower deficit should concessional financing fall short of the assumptions under the program. Despite losing one-time revenues from the tax amnesty in 2004 (1½ percent of GDP), we expect tax revenues to increase by ½ percent of GDP, reflecting already adopted fuel price increases, higher gas export volume and prices to Brazil and Argentina, and the full year impact of the FTT. Overall spending would decline by 0.3 percent of GDP in relation to 2004, notwithstanding the initiation of new important pro-growth projects, including key roads (¾ percent of GDP). These projects have been selected based on the highest quality standards, with World Bank advice on the needs for infrastructure, and principles of transparency and accountability. Current spending would decline by 0.3 percent of GDP in relation to 2004, while cuts in lower priority investment projects would contain capital spending at the 2004 level in percent of GDP.

7. We recently submitted to Congress an amended 2005 budget with a deficit of 5¼ percent of GDP, which we expect Congress to approve before end-June 2005 (structural PC). Moreover, should actual revenues fall short of projected levels, we would reduce expenditure levels to meet the fiscal deficit target. In addition, should tax revenues exceed programmed levels, we would increase spending levels, particularly on high quality, pro-growth and poverty reducing programs drawing on the recommendations from the recent World Bank-IDBs' public expenditure review and from the independent expenditure commission, by up to 66 percent of the gross tax revenue over-performance (before coparticipation).

8. We have adopted several measures to raise revenues on a sustainable basis, including:

- In January 2005, we raised excise taxes on fuel derivatives, including gasoline and diesel, with price increases by 10 percent and 15 percent, respectively. This should increase revenues by 1.0 percent of GDP, reduce subsidies by 0.2 percent of GDP, and help contain budget costs related to smuggling and poorly targeted subsidies. Prices of gasoline and diesel remain below regional averages and a recent poverty and social impact analysis (PSIA) suggests that the increases mainly affect upper-middle and high-income segments of the population. Nevertheless, in an effort to minimize the impact on vulnerable groups, we have maintained LPG subsidies; and we are strengthening our special employment program targeted to rural and poor areas.

- With Fund technical assistance, we are preparing a comprehensive tax reform to enhance revenue collection on a sustainable basis and improve the fairness of the system. Among other measures, we are considering the introduction of a personal income tax, which will exempt 80 percent of the population, and plan to hold consensus-building meetings with different sectors of society. We expect to submit to Congress draft legislation by September 2005 (benchmark, to be converted into a PC in the context of the next review, once we have determined the specific elements of the package). Approval by October 2005 would be a structural benchmark.

- A clear priority is to strengthen the Tax and Customs administrations. In particular, regarding Customs, we are implementing a comprehensive strategy towards reducing smuggling and corruption. Fund technical assistance has been requested for the first half of the year with respect to this and other initiatives to enhance Tax and Customs performance.

9. We are adopting several recommendations of the expenditure and pensions commissions aimed at containing and improving the composition of public expenditure:

- We intend to contain the increase in public sector wages below 3 percent. Increased efficiency in both the health and education sectors, with the aim of making progress towards the Millennium Development Goals, will be combined with restraint on new hirings so that the wage bill would decline by 0.3 percent of GDP compared to 2004. This would reduce crowding out of essential goods and services, and contribute to gradually bringing the wage bill as a percent of GDP to levels close to those in neighbor countries. We will complete a comprehensive survey and setup a registry on health and education sector employment by end-September, to reduce fraud and to increase accountability (benchmark). We intend to develop an action plan to reform the civil service, building on the recommendations from the World Bank-IDBs' Public Expenditure Review (PER).

- We recently issued a supreme decree with prudential norms to stop pension fraud, such as the 15,000 ineligible pensioners identified by the pension commission's report. We are committed to implementing the report's recommendations, which over time could reduce pension costs by up to 0.5 percent of GDP on an annual basis. The program conservatively assumes no savings in 2005.

- In line with the recommendations of the high-level expenditure commission, university subsidies will be limited to increase at most with inflation for the first time in several years, given the growing spending imbalances between the university and secondary education sectors.

- Excluding local governments, capital spending and transfers to the state oil company (YPFB) and other state agencies will remain at their 2004 level. To this end, in order to accommodate key new projects, including the Santa Cruz-Puerto Suárez road, we have reduced other projects, mostly financed with nonconcessional resources.

10. Given the challenges and risks associated with decentralization and the planned Constituent Assembly, we intend to take the following steps:

With Fund technical assistance, we are preparing an Organic Budget Law, which would set hard budget constraints at all levels of government and make the budget more transparent in defining fiscal priorities. The law will be submitted to Congress by June 2005 (benchmark) and we expect its approval by end-October 2005 (benchmark).

By September 2005, we expect to conduct an audit of subnational debts, and take immediate steps to help reduce municipalities' debt and improve expenditure monitoring, including: (i) implementing sanctions for breaking debt limits; (ii) improving the fiscal accounts at the national and local level by adopting a functional classification for public expenditure; and (iii) improving financial information systems, particularly through the creation of a debt registry, which will also track floating debt.

11. While the new tax code has been useful in increasing tax collection, we believe that the approval of a law regulating the appeals process defined in the code would reinforce the ability of the Tax Superintendency to enforce legislation. We expect the approval of the law to take place by June 2005 (a structural PC).

12. With funds pledged by the international community during the budget support meeting in late October in La Paz, we expect our 2005 fiscal program to be fully financed. As part of our commitments under the Multi-Donor Budget Support Program (PMAP), we will firmly pursue a number of measures to improve fiscal transparency. Should available financing fall short of the levels under the program, we stand ready to reduce spending or adopt revenue measures, including further restraint on current expenditure and cuts in lower priority investment projects.

C. Monetary, Debt and Exchange Rate Policies

13. End-2004 NIR exceeded the program target by around US$193 million, and reserve coverage increased by 8 percentage points to 39 percent of financial sector dollar deposits. Further, monetary policy will target an increase in NIR of the central bank, excluding deposits of financial institutions, of US$40 million in 2005, raising reserve coverage to 41 percent of projected dollar deposits. Should bank deposits further recover, we will aim at maintaining the reserve coverage of deposits.

14. We intend to strengthen and institutionalize our efforts to reduce debt vulnerabilities. During the second half of 2004, we were able to significantly increase gross placements in domestic currency and to lengthen their average maturity, in part by allowing the interest rate premium for one-year domestic over foreign currency bonds to increase by 300 basis points. However, with around 80 percent of domestic debt still dollar-denominated, and US$400 million falling due in 2005, significant vulnerabilities remain. Against this background, (i) we have established a debt management unit, with senior members from the

Central Bank and the Ministry of Finance, aimed at institutionalizing efforts to improve the structure of the debt, including setting targets for reducing short-term and indexed, or dollar-denominated debt, monitoring progress towards those goals and recommending changes to correct for any deviations; and (ii) we will, in line with the recommendations of this unit, further improve the currency composition and maturity of domestic debt throughout 2005, including through further increases in interest rates, as necessary. In addition, should market conditions allow us to engage in debt management restructuring operations, we are committed, in consultation with Fund staff, to further reduce the Treasury's debt with the central bank, and increase central bank net international reserves.

15. The crawling peg exchange regime has served Bolivia well in maintaining low inflation. In addition, Bolivia's competitiveness has improved markedly, in the context of the appreciation of neighboring countries' currencies. However, the limited flexibility of the exchange rate, which restricts its ability to deal with shocks, has been a source of concern. In this context, we plan to take advantage of recently introduced technological enhancements to improve the operation of the foreign exchange auction (*"Bolsín"*) before September 2005. While this system is not expected to alter significantly the operation of the current system, it will allow the central bank to purchase foreign exchange, when appropriate, and the exchange rate to better reflect market conditions.

D. Banking and Corporate Sectors

16. Financial system policies focus on reducing liquidity and solvency risks, and fostering economic growth by improving the efficiency of the financial system:

a. Bank Supervision has been strengthened through improved early warning systems to monitor liquidity and solvency risks. New regulations for effective supervision of financial conglomerates and improved banks' liquidity management were recently issued. Further, the 2005 on-site inspections, to start in May, are aimed at taking prompt corrective actions to strengthen vulnerable institutions.

b. We recently eliminated an essential element of prudential forbearance granted by previous administrations, by repealing supreme decrees that had relaxed provisioning requirements. The SBEF issued norms tightening loan classification and provision regulations, calling for gradual increases in provisions through May 2008, with the first effective increase to take place by end-May 2005. We plan to maintain current regulations regarding repossessed assets.

c. We have submitted to Congress an amendment to the banking law to establish the Financial Restructuring Fund (FRF) as a legal entity; to ensure appropriate financing for bank resolution processes through end-2005; and to consolidate the SBEF's regulatory and budgetary autonomy. We have also clarified by decree that the regulatory powers over the financial system lie with the BCB and the SBEF only, and plan to submit by September 2005 a bill creating a deposit insurance scheme, with partial deposit coverage and adequate financing (benchmark). To this end, we plan to request World Bank technical assistance to support joint efforts by the Ministry of Finance, the BCB, and the SBEF.

d. We will sell the state's participation in banks majority-owned by Nafibo, by end-December 2005 (structural PC).

e. We will submit to Congress draft legislation to improve the corporate restructuring and bankruptcy framework by end-September 2005 (benchmark), including through enhanced protection of creditor rights.

17. To further strengthen the prudential framework and induce banks to internalize risks associated with the high level of dollarization, the Central Bank plans to gradually increase reserve requirements on dollar deposits. The first increase will be about two percentage points in April on the average requirements (benchmark) and the effective rate will be stepped up by a cumulative amount of up to 3½ percent by September. The SBEF will require by August 2005 that financial institutions assess their exposure to credit risk derived from debtors' currency mismatches.

18. Projects to broaden the public sector role in the financial sector, through expanded activities of second-tier banks (including NAFIBO and FONDESIF), will be made within the existing fiscal program limits, avoiding subsidies, bailouts or special treatment of specific sectors. Moreover, the regulatory and supervisory framework (including entry, exit, internal control, prudential rules and governance aspects) of existing or new public financial institutions will be similar to the one applicable to private financial institutions.

E. Medium-Term Issues

19. The efficient exploitation of our large gas reserves is critical to enhance growth, reduce poverty, and achieve debt sustainability over the medium term. In this connection:

- Despite recent difficulties, we still expect Congress to adopt a hydrocarbons law in the coming months, which will allow us to adopt a strategy on gas exports by end-June 2005 (benchmark). A commission of notables has started working to: (i) facilitate and enrich discussions; and (ii) help us draft the regulations to provide additional and more specific safeguards for the proposed earmarked funds and their use according to strict principles of accountability and transparency. We are also interested in joining the UK's Extractive Industries Transparency Initiative (EITI).

- We are committed to the adoption of a framework consistent with increased gas exports and investment, addressing both the wishes of the population—as mandated by the gas referendum results—and the need to maintain an environment conducive to increased private investment.

20. More generally, we are committed to maintaining a general framework friendly to private investment, including respect of signed contracts, as we see the maintenance of the rule of law as critical for Bolivia's medium-term prospects.

21. Building on the current economic recovery, the government's objective is to achieve sustained growth of 4½–5 percent (about 2 percent per capita), making a significant dent in poverty levels over the medium term. We intend to pursue further fiscal consolidation to increase the availability of financing to the private sector, while boosting and better targeting pro-poor spending. We also plan to remove structural and institutional barriers to growth, including by improving transparency and governance, and advancing negotiations on free-trade agreements with our main trading partners to ensure access to foreign markets for Bolivian products.

22. We are fully committed to broadening consensus for the reform agenda both in Congress and amongst social and private partners. This consensus will be critical to secure approval by Congress of important reforms, including an appropriate hydrocarbons law, the budgets for 2005 and 2006, a suitable organic budget law, and tax reforms.

23. Through a participatory process with civil society, the National Dialogue was concluded in December 2004 to provide input for a new PRSP, which is still under preparation. We will ensure that the PRSP encompasses fiscal issues, including sustainable sources of fiscal revenue, well-targeted social safety nets, clear priorities for national spending, and ways to increase employment and reduce poverty. We have been holding meetings with the international community to exchange views on such strategy, and intend to hold a follow-up Consultative Group meeting later in the year.

Table 1. Bolivia: Quantitative Performance Criteria Under the SBA, 2004 1/

	2004		2005			
	Act.	Act.	Proj.	Performance Criteria		
	Sept.	Dec.	Mar.	June	Sept	Dec.
(Cumulative amounts from December 31, 2003 for the 2004 targets and December 31, 2004 for the 2005 targets; in millions of bolivianos)						
Deficit of the combined public sector 2/						
Unadjusted limit	2,556	4,032	676	1351	2123	3763
Adjusted limit	2,542	3,996				
Actual--projected	2,170	3,860				
Margin	372	136				
Net domestic financing of the combined public sector 3/						
Unadjusted limit	831	1,223	41	122	347	1174
Adjusted limit	534	926				
Actual--projected	370	1,035				
Margin	164	-109				
Central Bank Net Credit to the NPFS						
Unadjusted limit	-116	104	-166	-391	-298	137
Adjusted limit	-407	-187				
Actual--projected	-396	-360				
Margin	-11	173				
Net domestic assets of the central bank 4/						
Unadjusted limit	495	688	73	-168	-106	102
Adjusted limit	495	688				
Actual--projected 4/	10	-354				
Margin	485	1,042				
(Cumulative amounts from December 31, 2003 for the 2004 targets and December 31, 2004 for the 2005 targets; in millions of US dollars)						
Net international reserves of the central bank 5/						
Target	-104	-55	-90	-43	-21	40
Adjusted target	-104	-55				
Actual--projected 4/	-25	138				
Margin	79	193				
Net nonconcessional external debt 6/						
Limit	34	87	34.9	12.8	23.3	14.4
Adjusted limit	-28	5				
Actual--projected	-28	-4.7				
Margin	0	10				
External debt with maturities up to one year						
Limit	0	0	25	25	25	25
Actual--projected	-25	-25				
Margin	25	25				
(Cumulative amounts from December 31, 2003 for the 2004 targets and December 31, 2004 for the 2005 targets; in millions of US dollars)						
Adjuster to the nonconcessional external debt limit for financial and corporate restructuring						
WB and CAF nonconcessional financing for financial and corporate restructuring						
Program baseline	62	82	1	1	8	10
Actual--projected	0	0				
Adjuster to the net domestic financing of the NFPS						
Net external financing of the NFPS 7/						
Program baseline	172	289	70	128	188	273
Actual--projected	84	196				
Adjuster for the deficit of the SPNF						
Financing through HIPC and beyond-HIPC debt relief (program) 8/						
Program baseline	42	61	8	23	30	45
Actual--projected	41	56				
External financing for social spending						
Program baseline	0	0	0	0	0	0
Actual--projected	0	0				
Projected program grants						
Program baseline	18	45	0	3.8	3.8	45
Actual--projected	4	37				
Projected concessional program loans						
Program baseline	84	105	6.5	33.9	33.9	53.9
Actual--projected	51	88				
Tax Revenues						
Program baseline	...	...	439	966	1459	1948
Actual--projected						
(Cumulative amounts from December 31, 2003 for the 2004 targets and December 31, 2004 for the 2005 targets; in millions bolivianos)						
Maximum adjustment to limit on domestic financing of combined public sector						
Program baseline	500	500	500	500	500	500
Actual--projected	708	747				
Adjuster for NIR on currency issue						
Currency issue (program)	-338	246	-661	-518	-277	428
Maximum adjustment to NIR target	50	75	0	25	50	75

Source: Data provided by the Bolivian authorities.

1/ Definitions of the targets and adjusters as in the TMU of March 21, 2003 and the supplementary TMUs of June 2, 2004, September 23, 2004. September 2004 are PCs and December 2004 indicative targets set in Country Report No. 04/350. For the SBA extension, March 2005 are indicative targets and June, September, and December 2005 are proposed PCs.

2/ The limits on the deficit of the combined public sector will be adjusted downward by the difference between actual and projected program grants (i.e., grants not earmarked for projects). They will be adjusted downward (upward) by the amount of the shortfall (excess) between actual and projected HIPC debt relief and by the amount of the shortfall between actual and projected external financing for social spending, up to the designated ceilings. They will be revised downward by 33 percent of excess tax revenues over programmed levels.

3/ The limits on the net domestic financing of the NFPS will be adjusted upward by the difference between projected and actual net external financing to the NFPS (measured cumulatively over the same period as net domestic financing), excluding HIPC debt relief, up to the designated ceiling; it will be adjusted downward by the amount of any overdue obligations to foreign official creditors.

4/ The limits on the NDA of the BCB will be adjusted downward by the amount of any overdue obligations to foreign official creditors. The ceiling will be adjusted for the flow flow of the Central Bank financial system foreign deposits.

5/ The ceiling on NIR will be adjusted upwards by the amount of any overdue obligations to foreign official creditors and adjusted downward by shortfalls relative to the projected currency issue, up to the designated ceiling. The ceiling will be adjusted for the flow of the Central Bank financial system foreign deposits.

6/ The debt limit will be reduced by the amount, if any, of the shortfall between actual and projected disbursements of loans for financial and corporate restructuring.

7/ Does not include the HIPC debt relief through rescheduling or the amortization component of stock of debt reduction operations under HIPC Initiative and beyond HIPC.

8/ Comprises refinancing and the amortization component of stock of debt reduction operations under the HIPC Initiative and beyond HIPC, both for the financial and nonfinancial public sectors.

Table 2. Bolivia: Update of Status of Structural Conditionality For the Extension of the Stand-By Arrangement 2004[1,]

Condition	Policy Measure	Date	Comments
Public Sector Reform and Financing			
Performance Criterion	Approval by Congress of the law regulating the procedural requirements of the recursos de alzada and jerárquico before the Tax Superintendency.	September 30, 2004	Approved by the Upper House and awaiting approval of the Lower House of Congress. Now a PC for end-June, 2005.
Benchmark	Define terms of reference and appoint high-level commission of respected members of civil society	June 30, 2004	Observed. Commission appointed.
Performance Criterion	Publish high-level commission's report with specific recommendations, including measures to: (i) improve the measurement of pro-poor spending; (ii) improve the quality and efficiency of public services; (iii) prioritize spending toward growth-enhancing and pro-poor spending; and (iv) identify spending priorities to bring overall spending to a level of 32.1 percent of GDP in 2005, 31.0 percent of GDP in 2006, and 30.4 percent of GDP in 2007.	September 30, 2004	Observed. Commission published report.
Benchmark	Submission to Congress of a budget consistent with a deficit target after grants below 5½ percent of GDP, after including currently extrabudgetary funds and taking into account: (i) expenditure limits and revenue projections in the budget bill, together with the likely revenue yields of specific additional revenue measures to be proposed by the authorities; and (ii) the recommendations of the expenditure commission.	October 31, 2004	Budget submitted to Congress in September but inconsistent with program target. Approved on a lapse of time basis. Supplementary decrees were issued to make spending limits consistent with the program.

[1] References in the table are to the relevant paragraphs of the Technical Memorandum of Understanding (TMU) of March 21, 2003; June 20, 2003; September 24, 2003; and June 2, 2004.

Condition	Policy Measure	Date	Comments
Financial and Corporate Sector			
Benchmark	On banks majority-owned by NAFIBO, complete the write-offs of the shareholders capital and approve the implementation of a business plan for the next two years, which shall include re-privatization of the banks by December 2005.	September 30, 2004	Observed. Due diligence completed June 15, and business plan is finalized.
Benchmark	Superintendency of Banks and Financial Entities (SBEF) will: (i) issue a norm to ensure the effective supervision of financial conglomerates (in compliance with Basel core principle 20); and (ii) establish procedures to strengthen early warning indicators to identify individual and systemic bank vulnerabilities and apply prompt corrective actions.	October 31, 2004	Delayed but issued in December.
Benchmark	Complete study with IMF technical assistance to recommend measures to promote the use of domestic currency.	October 31, 2004	Observed and report issued in December.
Benchmark	The Superintendency of Banks will provide a diagnostic of banks to increase provisions and develop a related action plan.	October 31, 2004	Diagnostic completed in October and action plan completed by November. Plan includes modification to loan provisioning regulation.
Benchmark	In consultation with Fund Staff, amend the laws on banks and financial institutions to ensure that the FRF is established as a legal entity and allow that its contributions to the bank resolution process be temporarily complemented by contributions of the central bank in this context for 2005 only.	November 30, 2004	Not observed.
Benchmark	Drawing upon the implementation of the informal workout law to a sample of firms and submit to Congress, draft amendments to existing legislation and draft laws, including solvency and corporate restructuring law in order to strengthen creditor's rights, taking into account the principles stated in paragraph 15 of March 24, 2003 TMU.	November 30, 2004	Not observed.
Hydrocarbons law			
Benchmark[2]	Approval by Congress of a Hydrocarbons Law that adopts a strategy on gas exports based on the national referendum including issuing the implementing regulations, regulating the taxation of hydrocarbons and providing an appropriate framework for developing the large hydrocarbon reserves.	October 31, 2004	A bill being discussed in Congress. Now a SB for end-June, 2005.

[2] Denotes new conditionality added since the conclusion of the third review under the SBA on June 10, 2004.

Table 3. Bolivia: Structural Conditionality for the Extension of the Stand-By Arrangement 2005

Conditionality
Prior Actions taken Before Issuance of Board Documents
Fiscal Policy: • Issuance of a supreme decree reducing spending limits below the 2005 budget, consistent with a deficit target of the combined public sector of 5.2 percent of GDP after grants. • Submission to Congress of a revised budget consistent with the program deficit target and nonconcessional financing of 1.5 percent of GDP. ***Financial Sector:*** • Issuance of supreme decree to eliminate regulatory powers of the Ministry of Finance over the financial system. • Issuance of norms tightening loan classification and provision regulations, calling for gradual increases in provisions, with the first increase taking place by end-May 2005. • Submission to Congress of legislation establishing the Financial Restructuring Fund (FRF) as a legal entity.

Condition	Policy Measures Planned	Date	Comments
Public Sector Reform and Financing			
Performance Criterion	Passage of a revised budget law for 2005 with spending levels consistent with staff's revenue projections and the program deficit target after grants of the combined public sector of 5.2 percent of GDP.	June 30, 2005	
Performance Criterion	Approval by Congress of the law regulating the procedural requirements of the recursos de alzada and jerárquico before the Tax Superintendency.	June 30, 2005	
Benchmark	With Fund technical assistance, submit to Congress an Organic Budget Law that sets hard budget constraints on all levels of government guided by the principles of budget unity, transparency, comprehensiveness, and appropriations determined by Congress.	June 30, 2005	
Benchmark	Submission to Congress of a comprehensive tax reform, including the introduction of a personal income tax, which will exempt 80 percent of the population.[2]	September 30, 2005.	

[2] It is proposed to be converted to a performance criterion in the next review once more specificity can be determined.

Condition	Policy Measures Planned	Date	Comments
Benchmark	Complete a comprehensive survey and setup a registry on health and education sector employment , as well as an audit on sub-national debt, including floating debt, based on FAD TA.	September 30, 2005	
Benchmark	Submission to Congress of a 2006 budget with spending levels consistent with staff's revenue projections and a deficit target after grants for the combined public sector of 4.1 percent of GDP.	October 31, 2005	
Benchmark	Approval by Congress of an Organic Budget Law that sets hard budget constraints on all levels of government guided by the principles of budget unity, transparency, comprehensiveness, and appropriations determined by Congress.	October 31, 2005	
Benchmark	Approval by Congress of a comprehensive tax reform including the introduction of a personal income tax, which will exempt 80 percent of the population.	October 31, 2005	
Performance Criterion	Passage of the 2006 budget law with spending levels consistent with staff's revenue projections and a deficit target after grants for the combined public sector of 4.1 percent of GDP.	December 31, 2005	
Financial and Corporate Sector			
Benchmark	Increase average reserve requirements on dollar deposits of financial institutions by 2 percent.	April 30, 2005	
Benchmark	Submit a draft law creating a deposit insurance scheme with partial deposit coverage and establishing its proper functioning.	September 30, 2005	
Benchmark	Submit to Congress draft legislation to improve the corporate restructuring and bankruptcy framework, including through enhanced protection of creditor rights.	September 30, 2005	
Performance Criterion	Sale and transfer on final basis of the ownership of the state's participation in banks majority-owned by Nafibo.	December 31, 2005	
Hydrocarbons law			
Benchmark	Approval by Congress of a Hydrocarbons Law and its regulations, which should provide an appropriate framework for developing the large hydrocarbon reserves.	June 30, 2005.	

BOLIVIA—SUPPLEMENTARY TECHNICAL MEMORANDUM OF UNDERSTANDING

1. This technical memorandum supplements the technical memorandum of understanding of March 21, 2003 and the supplementary technical memoranda of understanding of June 2, and September 20, 2004. It outlines the quantitative targets and limits described below for 2005, which will be measured as cumulative flows from December 31, 2004 (Table 1). It refines definitions for existing quantitative targets for (performance criteria for June, September, and December) net domestic financing of the combined public sector. It also includes new adjusters on the deficit of the combined public sector and the net international reserves of the central bank (BCB).

Quantitative performance criteria

2. The definition of net domestic financing of the combined public sector in Table 2 of the technical memorandum of understanding of March 21, 2003 will be replaced by the following:

a) ***Net domestic financing of the combined*** *p**ublic sector (CPS), sum of:***

(i) Increase in the net claims of the domestic financial system on the NFPS (excluding deposits in the BCB related to foreign loans administered as trust funds;

(ii) Cash operating results before distribution to the treasury's account of the BCB;

(iii) Change in the NFPS liabilities to the private sector in the form of fiscal certificates;

(iv) Increase in the domestic floating debt of the NFPS (liabilities incurred for goods and services received but not yet paid for, excluding claims on and liabilities to other entities within the NFPS); and

(v) All borrowing by the NFPS; including net disbursements to the NFPS related to any new domestic debt instruments issued by the government and held outside the NFPS.

Valuation changes (due to changes in inflation) in the stock of domestic debt denominated in inflation-indexed units (UFVs) would be excluded from the computation of net domestic financing of the CPS.

Adjusters to the program

3. **New adjuster to the deficit of the combined public sector (CPS):** Should tax revenues of the CPS be higher than programmed (see adjuster for tax revenue in the PC Table), the quantitative performance criterion of the deficit of the CPS will be revised downward by 33 percent of the difference between actual and program outturns.

4. **New adjuster to the net international reserves of the central bank:** The quantitative performance criterion on net international reserves of the BCB will be adjusted

upward/downward by the net increase/decrease of the legally required and excess reserves denominated in foreign currency by financial institutions held with the BCB.

Information requirements

5. The treasury will remit to the Central Bank, on a weekly basis, information on all placements of treasury bonds other than open market operations, necessary to monitor the deficit of the combined public sector and net domestic financing of the CPS targets.