International Monetary Fund

Republic of Congo
and the IMF

Press Release:
IMF Executive Board Completes Second Review Under the Republic of Congo's PRGF Arrangement and Approves US$11.6 Million Disbursement
July 14, 2006

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

June 29, 2006

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

No. ____/MEFB/CAB

Brazzaville, June 29, 2006

The Minister of Economy,
Finance, and Budget

to:

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

Dear Mr. de Rato:

1. On behalf of the government of the Republic of Congo, I am pleased to submit herewith the Memorandum on Economic and Financial Policies (MEFP) for the second review of the three-year program supported by the arrangement with the International Monetary Fund (IMF) under the Poverty Reduction and Growth Facility (PRGF). This memorandum also presents quantitative and structural performance criteria for end-June and end-December 2006, as well as indicative quantitative and structural benchmarks for end-September 2006.

2. Economic progress achieved under the PRGF arrangement has helped us achieve the decision point under the enhanced HIPC Initiative, a milestone in the government's efforts to ease the debt burden weighing on the Congolese economy's growth potential. We would also like to thank other development partners that have already granted new financing to the Congo, as well as the Paris Club for providing debt relief on Cologne terms. We also hope, in the near future, to finalize an agreement with the London Club (also on Cologne terms), which would lead to the financing assurances required for IMF interim assistance and the HIPC completion point.

3. Overall, the implementation of the program supported by the PRGF arrangement yielded satisfactory results in 2005. Implementation of the structural measures helped to further strengthen transparency and governance in the oil sector, as well as overall management of the public finances. Nevertheless, we request waivers for the non-observance of two quantitative performance criteria at end-September 2005 (the floor on the primary fiscal balance, and on minimum payments of external arrears), as these were related to a large extent to the authorities' response to external events outside of the control of the government, did not affect the overall performance under the program, and corrective steps have been taken. In particular, the temporary slippage in the fiscal deficit at end-September was mostly reversed in the fourth quarter, even though the indicative benchmark on the floor for the primary fiscal balance was not met at end-December 2005. In view of the delay in completing the second review due to the protracted discussions on the HIPC decision point,

we also request a rephasing of the three-year arrangement under the PRGF and its extension by six months, to June 2008.

4. Since the completion by the IMF Executive Board of the first review of the program supported by the PRGF on August 1, 2005, we have become increasingly more aware of the importance of implementing reforms to strengthen governance. In this context, the government intends to undertake a series of measures, described in the attached memorandum, to increase transparency, fight corruption, and strengthen the management of the nation's oil resources.

5. Based on the positive results achieved so far and continued commitment to implement a strong economic and social program, consistent with the objectives outlined in the interim Poverty Reduction Strategy Paper (I-PRSP), we request the completion of the second review under the PRGF arrangement and the disbursement of the third tranche associated with this review.

6. We believe that the policies set forth in the attached Memorandum on Economic and Financial Policies (MEFP) are adequate to achieve the objectives of the program, but will take any other measures that may become necessary for this purpose. We will consult with the Fund before 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. We will also ensure that all data and information necessary for the monitoring of the performance under the PRGF arrangement will be provided to the Fund on a timely basis, in accordance with the attached Technical Memorandum of Understanding. The third review of the program supported by the PRGF arrangement with the IMF is expected to be completed by November/December 2006.

7. We are committed to disseminating the Memorandum on Economic and Financial Policies as well as the Technical Memorandum of Understanding, and we authorize the IMF to publish its staff report, after consideration by the Executive Board.

Sincerely yours,

/s/

Pacifique Issoïbeka
Minister of Economy, Finance, and Budget

Attachments: - Memorandum on Economic and Financial Policies
- Technical Memorandum of Understanding

Memorandum on Economic and Financial Policies for the Second Year Under the PRGF Arrangement

1. Poverty reduction continues to be at the core of our government's development strategy, as elaborated in the Interim Poverty Reduction Strategy Paper (I-PRSP) adopted in September 2004. The progress report on the I-PRSP produced in March 2006 shows continued progress on the preparation of a final PRSP—expected to be completed in the second half of 2006—following a participatory process involving the government, parliament, civil society, local communities, and development partners. The two main objectives of the government continue to be to stimulate growth and to promote pro-poor development. Our economic program is supported by the International Monetary Fund (IMF) with a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF), which was approved in December 2004. For the second review under the PRGF, this Memorandum of Economic and Financial Policies (MEFP) reviews performance under the program since the first review and describes the government's targets and policies for 2006 in particular.

I. Background

A. Recent Security and Economic Developments

2. The security situation has improved considerably in the context of a more relaxed political climate and the normal functioning of the key democratic institutions. The demobilization of former combatants, which has contributed to the improved situation, is ongoing with assistance from the World Bank. The next parliamentary elections are scheduled for 2007.

3. Macroeconomic developments in 2005 continued to be dominated by oil sector developments. Real GDP growth in 2005 is estimated at 7.9 percent, broadly in line with program projections, mostly reflecting favorable terms of trade, a strong pickup in oil production, and robust non-oil sector growth (especially in construction and public works, transport and communications, public administration and other services). Consumer price inflation moderated to 2½ percent in 2005 (year-on-year period average), following a decline of supply disruptions on the Pointe Noire-Brazzaville rail line that had pushed up inflation to over 3½ percent in 2004. Over the course of 2005, the real exchange rate depreciated slightly in line with lower inflation, and remains about 14 percent below its pre-1994 devaluation level. The external current account surplus rose sharply in 2005, to about 13 percent of GDP, mostly on account of a sharp increase in oil export receipts following the steep rise in the world market price for crude oil. Monetary developments in 2005 were marked by a strong buildup of deposits associated with the rise in oil revenues. Moreover, the increase in oil receipts clearly improved the fiscal situation as government expenditures have remained broadly under control.

B. Recent Performance under the PRGF-supported program

4. Overall, implementation of the PRGF-supported program produced satisfactory results over the period from April 1, 2005 to December 31, 2005. Most of the quantitative targets for end-June (benchmarks), end-September (performance criteria), and end-December 2005 (benchmarks) were met (see Table 1). In particular, all the performance criteria and quantitative indicators for end-September 2005 were observed, except for the ones on (i) clearance of external arrears and (ii) the primary fiscal surplus. Specifically,

- The minimum payments on external arrears clearance for end-September 2005 were missed, on account of the more favorable-than-programmed December 2004 Paris Club rescheduling agreement. However, the minimum payments for end-December 2005 were met. We have taken measures in the 2006 program to ensure that the performance criterion on the floor of arrears payments is consistent with the current agreements with creditors.

- At end-September 2005, the primary fiscal surplus fell short of its adjusted program target by a large margin (CFAF 112.9 billion, or 3.6 percent of GDP). This reflected three factors. First, with a view to protecting Congolese assets from litigating creditors, an amount of CFAF 83.3 billion (2.6 percent of GDP) in revenues from oil sales was received by the government, but not transferred to the Congolese Treasury before end-September 2005; these revenues were repatriated in their entirety by early November 2005 and were always under the control of the government. Second, an expenditure overrun of CFAF 18 billion was incurred owing to (i) higher-than-projected transfers to CORAF to cover the company's higher losses in the face of only partial adjustment of fuel pump prices, and (ii) the activation of government guarantees by private oil companies for their 2004 oil deliveries to CORAF that had remained unpaid. Third, although world oil prices were higher than programmed, raising the (adjusted) primary fiscal surplus target under the program, the positive revenue impact was partially offset by the sharp rise in the discount on Congolese crude oil associated with heavier demand for lighter crude in the world oil market and higher freight costs for West African oil. In addition, fees and commissions related to efforts to protect state oil revenues (noted above) increased by CFAF 10.2 billion (0.3 percent of GDP).

- At end-December 2005, the slippage in the fiscal balance was mostly reversed once the oil revenues were repatriated. The primary fiscal surplus was CFAF 669.7 billion (21.3 percent of GDP), somewhat below the (adjusted) indicative target under the program of CFAF 727.1 billion. This mainly reflected a short delay at the end of 2005 in the receipt of CFAF 27.4 billion in oil proceeds, which were transferred to the Treasury in early January 2006. The overall fiscal surplus, after debt service payments, was CFAF 501.3 billion (15.9 percent of GDP). We have provided IMF staff with a table identifying poverty-reducing spending relating to the 2005 budget execution and the 2006 budget.

5. The two structural performance criteria for end-September 2005 were observed. First, we adopted an action plan for the introduction of an automatic price adjustment mechanism for refined petroleum products. Second, the certification of forestry revenues in 2004 by an audit firm of international reputation was completed and the report was submitted to the government.

6. Moreover, most other structural benchmarks were observed through end-December 2005 (see Table 2). These include the adoption by the government of a strategy to refocus the activities of the SNPC on its core activities in the oil sector, along with an implementation timetable. The certification of oil revenues by an audit firm of international reputation for the third and fourth quarters of 2005 were also completed, and the related reports were published on the government's Internet site, although with a delay. The report on the diagnostic assessment of the 2004 losses of the refined petroleum products sector has not yet been completed, as we are awaiting the completion of a poverty and social impact analysis (PSIA) with financial assistance from the World Bank. The adoption of a comprehensive plan for the settlement of domestic arrears was delayed, due to protracted negotiations with trade unions on social arrears; however in November 2005 we adopted a plan for settlement of commercial arrears, and its implementation is well underway. The plan for settlement of social arrears is expected to be adopted shortly. The comprehensive plan for settlement of all domestic arrears will be posted shortly on the government's web site.

7. We took three important measures since the start of the year to further improve transparency in the oil sector. First, we launched an open and competitive bid for the audit of the process of awarding the Marine XI oil field concession in 2005, based on terms of reference acceptable to IMF and World Bank staffs. Second, we launched an open and competitive bid for a diagnostic study of SNPC's marketing strategy as a first step towards the adoption of international best practices for the sale of government oil—a trigger under the HIPC Completion Point. Third, we have published the certification report by an audit firm of international reputation of oil revenue for the fourth quarter of 2005, as for the other quarters of 2005, and the audit of the 2004 consolidated accounts of the SNPC. The latter states that the accounts are now auditable, reflecting significant improvements in access to information and internal controls, but are not yet certifiable according to international accounting standards.

8. Some progress was made toward strengthening the banking system and its privatization. First, an audit firm of international reputation completed an audit of the loan portfolio of COFIPA (the only remaining public commercial bank) as of June 30, 2005 (indicative benchmark for end-October 2005). However, the quarterly report on the financial situation of COFIPA (a continuous indicative benchmark) was not done on time, and the strengthening of the restructuring plan of the same bank was not carried out, as we were approached by a large reputable international bank for the privatization of COFIPA. In this context, we have launched a competitive bid for the recruitment of an independent consultant to (i) conduct a fair and unbiased valuation of the bank; (ii) assess the offer made by the potential buyer of the bank; and (iii) make recommendations to the government accordingly. Based on the COBAC's own independent rating system (SYSCO), the average quality of the

four banks in the Republic of Congo has improved from a fragile financial situation (3B) at end-2004 to a good financial situation (2) at end-2005, with one bank reaching the highest rating of a solid financial situation (1) at end-January 2006.

II. Key Macroeconomic and Poverty-Reduction Objectives for 2006 and The Medium-Term

9. Congo's medium-term economic prospects have improved significantly owing to sharply higher world oil prices. As a result, relative to the original program baseline scenario, the updated framework envisages higher oil revenues and investment spending and stronger GDP growth, as well as significant increases—associated with higher oil revenues—in the primary fiscal surplus and the external current account surplus. More specifically, the key changes to the medium-term macroeconomic framework are as follows:

- In view of higher investment spending, non-oil real GDP growth is expected to reach 6.3 percent in 2006 and about 6½ percent in 2007 and 2008.

- Domestic revenues are projected to reach around 40 percent of GDP in 2006 and to average about 39 percent of GDP in 2007/08.

- Pro-poor spending is expected to reach about 30 percent of total primary spending in 2006, and to increase further to 35.4 percent in 2007.

- The primary fiscal surplus is projected to be about 20 percent of GDP in 2006 and 2007/08. The non-oil primary deficit is projected to widen from 10.8 percent of GDP in 2005 to12.7 percent in 2006, and to average about 11½ percent in 2007/08.

- The current account surplus is projected at 14.0 percent of GDP in 2006, and to fluctuate around 14.0 percent of GDP in 2007/08.

10. We are committed to a prudent approach to using the oil proceeds deposited in a special revenue stabilization account at the central bank. The only permissible use for the resources in the oil account is to make transfers to the budget. The government will first consult with IMF staff before implementing additional expenditures not already envisaged in the current budget law. Any such expenditures will be authorized through a regular budget law or, in the event of an unforeseen expenditure need during the year, through a supplementary budget law. In addition, the proceeds in the stabilization account can be used to prepay expensive debt—specifically oil-collaterized loans and liabilities due to the BEAC—with a view to reducing the average cost of the debt; the net savings from these debt management operations would free up additional resources that can be used for poverty reduction over time. At the end of each year (starting from 2006), the oil account will be audited on a yearly basis by the national auditing office (Cour des Comptes) with a lag of no more than three months from the end of the year, and the audit report will be published on the government's web site.

11. In line with the understanding under the HIPC Decision Point, interim debt relief will also be saved in a special account at the central bank. Interim debt relief will only be used for poverty alleviation, and in particular for health and education spending. All spending will be approved through regular or supplementary budget laws, and will be reported to Fund staff in the context of program reviews. For 2006, the authorities do not envisage any spending out of this account until the final PRSP is completed (see below). Starting in 2007, this special account will be audited annually by the national auditing office (Cour des Comptes) and by an independent firm of international reputation with a lag of no more than three months from the end of the year, and the audit report will be published on the government's website. Accordingly, the transactions through the special account for 2006 will be audited by end-March 2007. The reports produced by the national auditing office and the audit firm of international reputation, as well as all other relevant information, will also be reviewed ex-post by a committee comprising government officials, parliamentarians, civil society, and donors, to make recommendations to the government.

12. Part of the higher expected fiscal revenues will be used to increase spending for poverty alleviation starting in 2007, in line with a medium-term budget framework consistent with the sustainable management of the country's oil resources. Regular updates of oil reserves and production schedules will be used to obtain reasonable estimates of the country's permanent income from oil, given that oil production is currently expected to decline sharply after 2010. Spending decisions for poverty alleviation will be targeted to reach the Millennium Development Goals (MDGs) and will be based on considerations of immediate pressing spending needs. The level of spending will take into account fiscal sustainability and absorptive capacity constraints, reflecting mostly a shortage of trained personnel in health and education and inadequate basic physical infrastructure.

13. As discussed in the progress report prepared in March 2006, work is underway on drafting the final Poverty Reduction Strategy Paper (PRSP). The participatory process for the final PRSP will be broadened and deepened by including the input of civil society and key stakeholders early in the design process. In addition, a donor coordination body has been set up to support the PRSP process and to facilitate donor participation. The final PRSP is expected to be completed in the second half of 2006.

14. A key objective of government policy is to re-orient public spending towards priority sectors identified in the interim PRSP and the final PRSP. To enable a more comprehensive poverty diagnosis, a poverty assessment was conducted in June 2005, and a national household survey was completed at end-2005. Steps are also being taken to strengthen the monitoring and evaluation system for the final PRSP. In particular, pending a comprehensive revision of the functional classification of government expenditures, we will continue to prepare quarterly tables tracking poverty-reducing spending. Starting with end-2006, we will also submit tables, on a quarterly basis, tracking the expenditure circuit (commitment, payment order, and cash payment); these tables will be verified by the Inspectorate-General of Finance. We have also requested technical assistance from the IMF's Fiscal Affairs Department on budget classification, in order to prepare the 2008 budget along functional lines.

III. The Policy Agenda For 2006

15. Against the background of the interim PRSP and with a view to making progress towards the Millennium Development Goals, our policy agenda for 2006 is aimed at ensuring robust growth and poverty reduction in the context of a stable macroeconomic environment; promoting private sector development; improving transparency and governance in the oil sector; and increasing the effectiveness of the public sector.

A. Fiscal Policy

16. The major fiscal policy objectives for 2006 under the PRGF-supported program are to: (i) strengthen the framework for mobilizing oil and non-oil revenues; (ii) raise pro-poor spending while taking into account absorptive capacity constraints; (iii) improve the quality of spending and strengthen the public expenditure management system; (iv) begin to design a medium-term budget framework consistent with sustainable management of the country's oil resources; (v) accelerate the settlement of government payments arrears and increase government deposits at the *Banque des Etats d'Afrique Centrale* (BEAC); and (vi) reduce losses in public enterprises.

17. The government undertakes to further strengthen the framework for mobilizing oil and non-oil revenues:

- On oil revenues, we will continue our efforts to ensure that all private oil companies meet their tax obligations in a timely manner. The government has examined the amount of oil revenue shortfalls identified by the 2003 cost oil audits, estimated at about US$150 million, and has initiated the legal procedures for settling the amounts outstanding. Other measures for oil revenue mobilization will include:

  - continuation of the quarterly certification of oil revenues by an internationally recognized audit firm, and without qualification on access to information;

  - commissioning a reconciliation report on the amount of oil revenues deposited in government bank accounts, as reported in the quarterly certification reports, and total oil revenues reported in the government financial operations tables (TOFEs) for 2005 without qualification on access to information. This report will be submitted to the government (performance criterion for end-June 2006) and published on the Internet site of the Ministry of Economy and Finance (www.mefb-cg.org);

  - commissioning an independent audit of cost oil for all production-sharing contracts, based on international standards and carried out by internationally recognized audit firms, for 2004 and 2005. These cost audits will be carried out by December 31, 2006, at the latest, and published on the Internet site of the Ministry of Economy and Finance (www.mefb-cg.org); and

- ➢ completion of a diagnostic study, by an independent firm of international reputation, of the economic viability of the CORAF, which will be submitted to the government before end-October 2006.

- On non-oil revenues, we will focus on measures to strengthen tax administration (accelerate the computerization of the tax and customs administrations; combat fraud and tax evasion; and refrain from approving any new discretionary tax and customs exemptions). We have commissioned an organizational audit of customs administration. Based on the recommendations of the audit, we will implement an action plan to strengthen customs administration, including the completion of the installation of the SYDONIA system. Moreover, we will continue with the annual certification of forestry revenues, by an audit firm of international reputation, using the same terms of reference as for the 2004 certification.

18. Expenditure policy will focus on poverty reduction. Domestically-financed current and capital outlays in 2006 are expected to increase by about 10 percent and 43 percent, respectively (relative to the outturn for 2005), a level that is likely to exhaust the country's absorptive capacities. This sharp rise in domestically-financed capital spending results from the very weak mobilization of external resources for investment expenditures. We intend to raise the share of pro-poor spending from 24.8 percent of total spending (4.9 percent of GDP) in 2005, to 29.9 percent of total spending (6.1 percent of GDP) in 2006, and to 35.4 percent of total spending (6.7 percent of GDP) in 2007. Our fiscal program also envisages an adjuster for up to CFAF 50 billion (1.5 percent of GDP) for additional priority investment projects vetted by the World Bank that would be awarded through transparent and competitive procurement procedures and approved through a supplementary budget.

19. Expenditure management priorities will focus on a number of issues. There will be more rigorous evaluation and monitoring of projects included in the 2006 investment budget, and greater transparency with regard to the implementation of these projects. A new procurement code is expected to come into effect by September 2007 to bring procurement practices in line with international best practices. The ongoing work to introduce a functional classification on government spending will be accelerated with technical assistance from the IMF, mainly to help identify and track pro-poor spending. We envisage monitoring the execution of the 2007 budget using a functional classification system consistent with the IMF's 2001 *Government Finance Statistics* manual —in addition to the usual classification— and to prepare the 2008 budget on the basis of this classification. In addition, the 2007 budget will present a three-year budgetary framework, where the 2008–10 projections will give a general indication of the government's fiscal policy over the medium term. The medium term budgetary framework will also present a section on pro-poor spending that will be in line with the priorities identified in the final PRSP.

20. Pending the adoption of a medium-term budget framework (as discussed above), we intend to be prudent in the use of oil revenues. Part of the higher projected oil revenues will be used to accelerate the clearance of domestic arrears, to prepay expensive domestic debt, to settle commercial external arrears, and to pay off expensive oil-collaterized loans. Beyond

the clearance of arrears, all additional oil revenue windfalls will be deposited in the stabilization account at the BEAC, in line with the commitments described above.

21. We will also undertake major reforms to address structural weaknesses in key sectors of the economy (fuel, electricity, and banking), which will improve efficiency and limit potential costs on future budgets:

- We remain committed to the introduction of an automatic price adjustment mechanism for refined petroleum products. The poverty and social impact analysis (PSIA) of such a measure is being undertaken with financial support from the World Bank. In the meantime, however, the implicit subsidy associated with fixed domestic prices grew in 2005 to CFAF 47.3 billion (about 1½ percent of GDP). Against this background, we decided in June 2006 to increase gasoline, diesel, and jet fuel prices by 11 percent, which will reduce implicit subsidies to CFAF 18 billion (0.5 percent of GDP) in 2006 on an annualized basis. We will adopt a timetable by end-September 2006 for the elimination of all implicit subsidies for refined petroleum products within one year. At that time, an automatic price adjustment mechanism will be introduced with a view to keeping domestic refined petroleum product prices in line with world market prices.

- We have already started the restructuring of the electricity sector. In particular, these operations include the implementation of a plan to install 50,000 electric meters in Brazzaville and Pointe Noire, which will improve the financial condition of the electricity company and includes an implicit increase in tariffs. We have also started a study of the electricity sector with the help of the World Bank in order to define a plan of action to improve the capacity of the sector and to rationalize tariffs. The investments associated with this plan of action will be integrated in the 2007 budget.

- We will ensure that the privatization of COFIPA is carried out in a manner that preserves the best economic and financial interest of Congo. Based on the report from our consultant, we will decide on how to proceed with the privatization of COFIPA on the basis of the economic fairness and budgetary implications of all the offers to be received by the government by end-August 2006. The consultant's report will be published on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org), following the sale of the bank.

22. In order to make progress with other necessary economic and social reforms, we have decided to undertake this year a major reform of the civil service on the one hand, and on the other hand the restructuring of the two pension funds, whose financial situation is fragile. Thus, we intend to commission an independent firm of international reputation, selected through an open bidding process, to undertake a census of civil servants and of civil service pensioners. Accordingly, we will start the process of establishing computerized records for all civil servants and civil service pensioners. We will also recruit an independent firm of international reputation, selected through an open bidding process, to help put in place modern systems of accounting and internal controls at the pension funds. Actuarial studies

will be undertaken to enable the government to prepare comprehensive restructuring plans for the two pension funds, to be implemented starting in 2007. On the budgetary front, we commit to reforming the Budget Directorate so as to improve its organization and the procedures for preparing the budget, to reviewing and streamlining the procedures for budget execution, to introducing a functional classification for public expenditures, and to ensuring the computerization of operations and the training of staff. Those actions which affect only one part of the expenditure chain will be implemented in the next stage through a reform of the public treasury.

B. Oil Sector Reforms and Transparency

23. We are committed to undertaking steps to improve governance and fiscal management in the oil sector. In this context, the financial audit of the national oil refinery CORAF for 2003 and 2004, by an audit firm of international reputation, has been completed, and the final report on the diagnostic assessment of the 2004 losses of the refined petroleum products sector will be ready by September 2006. Other measures have been described above.

24. We will adopt the following measures to ensure that the national oil company, the SNPC, undertakes its fiscal agency functions more effectively:

- Mandate an independent certification by the national auditing office (Cour des Comptes) that no members of the Executive Board of the SNPC or those having management responsibilities within the SNPC and its subsidiaries, at the moment of their nomination and annually thereafter, have any participation or other interests in companies doing business with the SNPC or its subsidiaries. This report will be submitted to the government (performance criterion for September 2006) and published on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).

- Adopt an action plan by end-February 2007 to bring the SNPC's marketing of government oil up to international standards, based on the diagnostic study expected to be completed in December 2006. This will be the next step towards the adoption of international best practices for the marketing of oil, a trigger for the achievement of the HIPC completion point.

25. We will continue to increase the amount of information made available to the public on its websites (www.mefb-cg.org and www.congo-site.cg), including the publication of (i) oil revenue certification reports; (ii) reconciliation reports on the amount of oil revenues deposited in government bank accounts, as reported in the quarterly certification reports, and the total oil revenues reported in the government financial operations tables (TOFEs); (iii) cost oil audits for all production-sharing contracts; (iv) external audit reports on the SNPC and CORAF; (v) laws and regulations governing relations between the state and the SNPC; and (vi) key oil sector-related data.

C. Other Governance Issues

26. Fighting corruption remains key to ensuring good governance. Thus, we will set up an anti-corruption committee that will play a central role in advancing the governance agenda and provide domestic leadership in this critical area. Moreover, we will submit to parliament, before end-2006, a comprehensive anti-corruption law which will, among other things, define conflict-of-interest and financial disclosure rules for public officials, to ensure that: (i) senior public officials (including in the government, civil service, and public enterprises) disclose, at the time of their nomination and annually thereafter, their wealth and the origins of their incomes; and (ii) the annual disclosure statements are reviewed by the national auditing office (*Cour des Comptes)* and certified by the national anti-corruption committee. The anti-corruption committee should publish a summary report on its findings within six months of the end of the calendar year. We also intend to make fully operational the national anti-corruption committee and the national auditing office (*Cour des Compte*s) by end-September 2006.

27. Strengthening governance and transparency in public resource management is a key objective of the government. In this context we plan to publish, by end-September 2006, the audit report on the awarding of the 2005 Marine XI oil field concession. Moreover, the government reaffirms its commitment to abide by the principles of the Extractive Industries Transparency Initiative (EITI). An EITI workshop with civil society and oil companies was convened by the government in September 2005, during which an EITI committee was formed, and a government website (www.mefbcg.org/eiti.htm) was launched with information on EITI implementation in Congo. A national EITI consultative committee and a national EITI executive committee will be established shortly by Presidential decree, comprising representatives from civil society and Parliament, in line with EITI recommendations. The consultative committee will be under the authority of the Prime Minister's office. The newly formed committee is currently in the process of defining its work program, with a view to publishing its first EITI report by end-December 2006. To bring the Republic of Congo back into the Kimberley Process for the certification of diamonds, from which it was excluded in June 2004, we have submitted three reports by independent experts on: (i) the 2005 production of raw diamonds in the Congo; (ii) the potential diamond reserves in the Congo; and (iii) the amendments to the mining law approved in 2005 to bring the law in conformity with the Kimberley process. A final onsite inspection by two experts commissioned by the Kimberley process committee is expected before June 2006. Based on their evaluation, we expect a decision on the reintegration of the Congo into the Kimberley process before end-2006.

D. Monetary and Financial Sector Issues

28. Monetary policy will continue to be conducted regionally by the BEAC. The key objectives remain unchanged, namely to ensure low inflation and to maintain the CEMAC region's foreign exchange reserves at a comfortable level.

29. The soundness of the Congolese financial system is essential to foster higher economic growth. In this respect, we have fully implemented the action plan for strengthening the recovery of the banking system's nonperforming loans. This includes the circulation by banks, on a quarterly basis, and with a one-month lag, a list of the principal delinquent debtors of the Congolese banking system to banking establishments and the public treasury. The public treasury will continue to collect on behalf of banks the amounts due from delinquent debtors, by deducting them from public procurement payments owed to them.

E. External Debt Management

30. We are continuing our efforts to normalize relations with external creditors. All external liabilities have been honored on time since the introduction of the PRGF-supported program. The Paris Club granted flow rescheduling on Cologne terms in May 2006, which applies to qualifying debt with maturities falling due between March 2006 and September 2007. We are considering different proposals for debt relief from London Club creditors, on comparable terms to the Cologne terms granted in May 2006 by the Paris Club, and hope to reach an agreement in the near term. We are also continuing discussions with all other bilateral and commercial creditors to seek comparable treatment.

F. Trade Policy Reforms

31. We are committed to further transparency in the application of our trade regime. As such we will publish on the internet the full list of tariff rates, the list of tariff lines that are subject to import licensing requirements and prohibitions, as well as those subject to exemptions and special excises.

IV. Program Monitoring and Data Provision

32. Program execution will be monitored by means of the performance criteria and quantitative and structural benchmarks specified in Tables 3 and 4 and described in the attached TMU. To enable the government to properly implement its poverty reduction program, quantitative and structural performance criteria have been set for end-June and end-December 2006, and indicative quantitative and structural benchmarks for end-September 2006. Definitions and other details on these benchmarks are provided in the attached TMU.

33. We will continue to provide information to IMF staff on a timely basis, as specified in the TMU, through the IMF resident representative office in Brazzaville. We will also provide any additional information that may be required to assess macroeconomic developments and program performance.

Table 1. Republic of Congo: Quantitative Criteria and Indicators , October 2004 - December 2005
(In billions of CFA francs, unless otherewise indicated; cumulative from January)

	End-Mar. 05			End-Jun. 05			End-Sep. 05				End-Dec. 05		
	Perf. crit.	Adj. perf. crit.	Est.	Benchmark	Adj. prog.	Est.	Perf. crit.	Rev. perf. crit.	Adj. perf. crit.	Est.	Indic. bench.	Adj. prog.	Est.
Quantitative criteria													
Primary fiscal balance (floor) 1/ 2/	98.8	64.3	96.1	163.6	219.7	210.9	230.4	230.4	427.0	312.7	473.9	727.1	668.7
Change in net claims of the banking system on the government (ceiling) 2/ 3/	1.8	1.8	-24.4	2.3	2.3	-42.3	4.0	4.0	4.0	-34.3	-30.0	-30.0	-237.0
New medium or long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (ceiling) 4/ 5/ 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
New external debt (including leasing) with an original maturity of less than one year (ceiling) 5/ 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
New oil-collateralized external debt contracted by or on behalf of the central government (ceiling) 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
New nonconcessional external debt contracted by SNPC (ceiling) 6/	13.5	13.5	0.0	13.5	13.5	0.0	13.5	13.5	13.5	0.0	13.5	13.5	0.0
External arrears payment (floor) 2/ 7/	60.2	60.2	44.4	108.5	108.5	99.8	119.6	113.1	113.1	105.0	134.0	134.0	149.4
New external arrears on nonreschedulable debt 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic arrears payment (ceiling) 8/ 9/	8.0	8.0	7.3	17.8	17.8	14.6	34.8	34.8	34.8	24.8	60.0	60.0	67.1
New domestic arrears 6/ 8/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Quantitative indicators													
Non-oil revenue	45.3	45.3	54.2	101.1	101.1	111.0	155.7	155.7	155.7	156.7	219.3	219.3	220.0
Domestically-financed investment (ceiling)	39.1	39.1	30.6	82.2	82.2	80.3	115.3	115.3	115.3	115.2	153.1	153.1	153.9
Memorandum items													
Oil revenue (in billions of CFA francs)	183.1	148.6	157.4	338.5	394.7	387.9	486.1	486.1	682.7	585.3	793.7	1047.0	1019.8
Petroleum price (Brent,US$/barrel), quarterly average	34.5	…	41.5	33.5	…	51.6	32.8	32.8	…	61.5	46.3	…	57.0
Exchange rate (CFAF/US$), quarterly average	544.4	…	498.4	543.7	…	524.1	543.1	543.1	…	537.6	499.7	…	552.5
Petroleum price Brent (thousand CFAF/barrel), quarterly average	18.8	…	20.7	18.2	…	27.0	17.8	17.8	…	33.1	23.1	…	31.5

1/ See paragraph 6 of the technical memorandum of understanding (TMU) (Country Report 05/07; Appendix I, Attachment III) for the definition.
2/ See paras. 23-25 of the TMU on the adjustors.
3/ Excluding IMF credit.
4/ Excluding rescheduling arrangements and disbursements from the IMF.
5/ See para. 13.b of the TMU for the definition of concessional debt.
6/ Continuous performance criterion; see para. 17 of the TMU for the definition of nonreschedulable debt.
7/ Excluding cancellation of arrears to the European Union, cancellation of part of arrears by the African Development Bank (AfDB), and clearance of arrears of Congolese Embassies abroad. The revised performance criterion for end-September 2005 and indicative benchmark for end-December 2005 exclude all arrears repayments to the AfDB, given that donors made firm pledges to pay the remaining one third of these arrears.
8/ See para. 21 of the TMU for the definition.
9/ See para. 26 of the TMU for the adjustor.

Table 2. Republic of Congo—Structural Performance Criteria, Benchmarks, and Indicators, April-December, 2005[1]

Measures	Date	Implementation Status
1. Structural performance criteria		
Preparation by the government and submission to the IMF of a table tracking poverty-reducing spending in 2004.	June 30, 2005	Done
Adoption by the government of an action plan (including a timetable) for the introduction of an automatic price adjustment mechanism for refined petroleum products.	September 30, 2005	Done
Certification of forestry revenues in 2004 by an audit firm of international reputation, and submission of the report to the government.	September 30, 2005	Done
2. Structural benchmarks		
Preparation by the SNPC of a statement of sources and uses of funds for the consolidated activities of the SNPC group for 2004, and quarterly tables for 2005.	June 30, 2005	Done
Adoption by the government of a definitive strategy to refocus the activities of the SNPC on its core activities in the oil sector along with the related implementation timetable.	September 30, 2005	Done
Adoption by the government of a comprehensive plan for the settlement of domestic arrears; posting of the related policy on an Internet site.	September 30, 2005	Not done[2]
Quarterly publication on the Internet of the recipients of domestic debt payments.	With one-month lag	Done
Quarterly certification of oil revenue by an audit firm of international reputation using the same terms of reference as for the 2003 certification; certification reports to be published on Internet sites.	With one-quarter lag	Not Done[3]
Publication on Internet sites of a detailed statement of all hydrocarbons transactions (oil and gas).	With one-month lag	Done
Centralization of all public revenues and execution of all public payments by the Treasury.	Continuous	Not done[4]
3. Indicative benchmarks[3]		
Completion, by an audit firm of international reputation, of a general audit of the statement of the COFIPA loan portfolio as of March 31, 2005.	October 31, 2005	Done

Table 2. Republic of Congo—Structural Performance Criteria, Benchmarks, and Indicators, April-December, 2005[1]
(Concluded)

Measures	Date	Implementation Status
Preparation by the government, with the help of the Central African Banking Commission (COBAC), of an action plan for strengthening the recovery of the banking system's nonperforming loans.	November 30, 2005	Done
Completion, by an audit firm of international reputation, of the establishment of the 2004 financial accounts of the National Electricity Company (SNE) in accordance with the standards of the regional business law harmonization agency (OHADA).	December 31, 2005	Not Done
Completion, by an audit firm of international reputation and in accordance with international standards on auditing, of the financial audit of the national refinery company (CORAF) for 2003 and 2004, and submission of the report to the government.	December 31, 2005	Done
Completion of the final report on the diagnostic assessment of the losses recorded by the refined petroleum products sector in 2004.	December 31, 2005	Not done
Preparation of a quarterly report by the government, in cooperation with the Central African Banking Commission (COBAC), on the financial situation of COFIPA following a site visit.[5]	With a one quarter lag	Not done[6]

[1] The measures are described in the technical memorandum of understanding (see IMF Country Report no. 05/7; January 2005).

[2] The government adopted and started implementing a settlement plan for commercial arrears, but has not yet adopted one for social arrears.

[3] The certification report for the third quarter of 2005 was published on the Internet in mid-February, instead of end-December 2005.

[4] The recent forestry revenue audit found that a formal administrative instruction (Lettre circulaire no. 0877/MEFE/MEFB) requires the direct payment of about 40 percent of forestry revenues to the Forestry Fund. However, this instruction was rescinded in December 2005 (Prime Minister's decree no. 7702/PMCAGP-CAB dated December 5, 2005).

[5] The reports will assess the solvency, profitability, and liquidity of this bank, as well as the implementation of the recommendations set forth in the report of October 18, 2004 entitled "COFIPA Investment Bank Congo : Evaluation and Restructuring."

[6] COBAC undertook its first on site visit in December 2005 and communicated its report to the authorities with delay.

Table 3. Republic of Congo: Tentative Quantitative Criteria and Indicators, March - December 2006
(In billions of CFA francs, unless otherewise indicated; cumulative from January) 1/

	End-Mar. 06 Proj.	End-Jun. 06 Perf. crit.	End-Sep. 06 Benchmark	End-Dec. 06 Perf. crit.
Quantitative criteria				
Primary fiscal balance (floor)	174.7	262.3	442.5	686.8
Change in net claims of the banking system on the government (ceiling) 2/	-79.6	-86.5	-191.0	-362.5
New medium or long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (ceiling) 3/	0.0	0.0	0.0	0.0
New external debt (including leasing) with an original maturity of less than one year (ceiling) 4/	0.0	0.0	0.0	0.0
New oil-collateralized external debt contracted by or on behalf of the central government (ceiling) 4/	0.0	0.0	0.0	0.0
New nonconcessional external debt contracted by SNPC (ceiling) 4/	0.0	0.0	0.0	0.0
External arrears payment (floor) 5/	28.3	56.3	84.2	112.4
New external arrears on nonreschedulable debt 4/	0.0	0.0	0.0	0.0
Domestic arrears payment (ceiling)	21.8	43.5	65.3	87.0
New domestic arrears 4/	0.0	0.0	0.0	0.0
Quantitative indicators				
Non-oil revenue	59.9	119.8	179.7	239.6
Domestically-financed investment (ceiling)	43.2	150.0	196.0	216.0
Memorandum items				
Oil revenue (in billions of CFA francs)	276.5	548.9	834.0	1127.8
Petroleum price (Brent,US$/barrel), quarterly average	61.0	60.0	61.5	62.5
Exchange rate (CFAF/US$), quarterly average	547.8	549.7	549.7	549.4
Petroleum price Brent (thousand CFAF/barrel), quarterly average	33.4	33.0	33.8	34.3

1/ All definitions of the quantitative performance criteria and corresponding adjusters are specified in the attached technical memorandum of understanding.
2/ Excluding IMF credit.
3/ Excluding rescheduling arrangements and disbursements from the IMF.
4/ Continuous performance criterion.
5/ Payments of consolidated arrears on post-cut-off date debt to the Paris Club creditors.

Table 4. Republic of Congo–Prior Actions and Structural Performance Criteria and Benchmarks for the Second Program Year

Measures	Date
1. Prior actions	
Certification without qualification on access to information of oil revenue for the fourth quarter of 2005 by an audit firm of international reputation using the same terms of reference as for the 2003 certification; certification reports to be published on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	Actions to be taken prior to issuing the staff report and letter of intent to the IMF Executive Board for consideration of the second PRGF review.
Completion, by an audit firm of international reputation, of the establishment of the 2004 financial accounts of the National Electricity Company (SNE) in accordance with the standards of the regional business law harmonization agency (OHADA).	
Launch the bid for the recruitment by the government of an independent consultant to conduct the valuation of COFIPA bank, provide an independent opinion about the offers received for the sale of COFIPA, the budgetary implications of these offers and make appropriate recommendation to the government. The consultant's report will be the basis for the government's decision on the privatization of COFIPA.	
Launching by the government of an open and competitive bid for an audit, by an independent firm of international reputation, of the process of awarding the Marine XI oil field concession in 2005, based on a terms of reference acceptable to IMF staff.	
Launching by the government of an open and competitive bid for a diagnostic study, by an independent firm of international reputation, of the SNPC's marketing strategy of government oil, including description of intermediaries used and costs incurred. The diagnostic study will be based on terms of reference satisfactory to IMF staff.	
Adoption by the government of a comprehensive plan for the settlement of domestic social arrears; posting of the related policy on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	Actions to be taken 5 days prior to Board consideration of the review.
Completion, by an audit firm of international reputation, of a reconciliation report on the amount of oil revenues deposited in government bank accounts, as reported in the quarterly certification reports, and the total oil revenues reported in the government financial operations tables (TOFEs) for 2005, without qualification on access to information; submission of the report to the government, and publication on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	

Table 4. Republic of Congo–Prior Actions and Structural Performance Criteria and Benchmarks

for the Second Program Year (continued)

Measures	Date
2. Structural performance criteria	
Completion of a certification report by the national auditing office (*Cour des Comptes)* that public officials (both in the government and at public enterprises) are not personally benefiting from government oil sales by the SNPC or its subsidiaries, and submission of the report to the government; publication of the report on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	September 30, 2006
Completion, by an independent firm of international reputation, of a diagnostic study of the SNPC's marketing strategy of government oil; submission of the report to the government.	December 31, 2006
3. Structural benchmarks	
Publication on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org) of the audit report of the awarding of the Marine XI oil field concession in 2005.	September 30, 2006
Adoption of a timetable for the elimination of all implicit subsidies for refined petroleum products within one year.	September 30, 2006
Establishment—i.e., adoption of the terms of reference and staffing—of an anti-corruption committee, whose terms of reference and composition will be satisfactory to IDA and IMF staffs.	September 30, 2006
Completion, by an independent firm of international reputation, of a diagnostic study of the economic viability of CORAF, and submission of the report to the government, based on terms of reference satisfactory to IMF staff.	October 31, 2006
Completion, by audit firms of international reputation and in accordance with international standards, of audits of oil costs for 2004 and 2005, for all production-sharing contracts as defined in these contracts, and submission of the reports to the government. Publication of the audits on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	December 31, 2006

Table 4. Republic of Congo–Prior Actions and Structural Performance Criteria and Benchmarks for the Second Program Year (concluded)

Measures	Date
Submission to Parliament of a draft "Anticorruption Law", that includes, among others, conflict-of-interest and financial disclosure rules for public officials. The financial disclosure rules would cover that: (i) senior public officials (including in the government, civil service, and public enterprises) must disclose their wealth and origins of their incomes when acceding to the post and on an annual basis; and (ii) the annual disclosure statements are to be declared to the national auditing office (Cour des Comptes) and certified by the national anti-corruption committee. The anti-corruption committee should publish a summary report on its findings within six months of the end of the calendar year.	December 31, 2006
Centralization of all public revenues and execution of all public payments by the Treasury.	Continuous
Quarterly certification of oil revenue by an audit firm of international reputation, using the same terms of reference as for the 2003 certification and without qualification on access to information; certification reports to be published on the Internet site of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	With one-quarter lag

REPUBLIC OF CONGO

Technical Memorandum of Understanding

Brazzaville, June 2006

1. This technical memorandum of understanding (hereinafter the "TMU") sets out the modalities for monitoring the program covering the period from April 1, 2006 through December 31, 2006 of the government of the Republic of Congo.

V. Quantitative Performance Criteria

2. The quantitative performance criteria are:

   a. a floor on the primary fiscal balance, cumulative starting from January 1, 2006,

   b. a ceiling on the change in the net claims of the banking system on the government (excluding net IMF credit), cumulative starting from January 1, 2006,

   c. no new medium- or long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (a continuous criterion),

   d. no new external debt (including leasing) with an initial maturity of less than one year incurred or guaranteed by the government (a continuous criterion),

   e. no new oil-collateralized external debt by or on behalf of the government (a continuous criterion),

   f. a ceiling on new nonconcessional external debt contracted by the SNPC with or without government guarantee, starting from January 1, 2006 (a continuous criterion),

   g. minimum external arrears payment, starting from January 1, 2006,

   h. no new external payment arrears on nonreschedulable external debt (see paragraph 17 below for the definition), starting from January 1, 2006 (a continuous criterion),

   i. a ceiling on domestic arrears payments, starting from January 1, 2006; and

   j. no new domestic payment arrears, starting from January 1, 2006 (a continuous criterion).

3. The quantitative indicators are:

a. a floor for non-oil revenues (cumulative amounts, starting from January 1, 2006), and

b. a ceiling on domestically-financed domestic investment (cumulative, starting from January 1, 2006).

VI. Definitions and Computation

A. Government

4. Unless otherwise indicated, "government" is defined as the central government of the Republic of Congo and does not include local governments, the central bank, or any public entity with autonomous legal personality not covered by the government's consolidated financial operations table (tableau des opération financières de l'Etat—TOFE).

B. Basic Primary Fiscal Balance

5. The scope of the government's fiscal operations table (TOFE) includes the general budget and the special accounts of the Treasury (including the forestry and road funds) and the government debt management agency (Caisse Congolaise d'Amortissement, CCA).

6. The government's basic primary fiscal balance is equal to total revenue excluding grants, minus total expenditure (including net credit) excluding interest payments and capital expenditure financed with external resources. It is measured on the basis of the budget execution reported every month in the TOFE prepared by the Ministry of Finance. At end-December 2005, the basic primary fiscal balance was estimated at CFAF 668.7 billion, resulting from total revenue (excluding grants) of CFAF 1239.8 billion and total expenditures (excluding interest on the debt and capital expenditure financed with external resources) of CFAF 570.10 billion.

7. The government's total revenue is measured on a cash basis. It includes all revenue collected by the Treasury (mainly tax revenue and customs duties, oil revenues, forestry revenues, and service charges), whether the result of past, current or future obligations. Total revenue also includes gross revenue in the special accounts. These are recorded on a gross basis. Oil revenue excludes all forms of prepayment and prefinancing (see definitions in paragraphs 18-19 below).

8. Starting January 1, 2006, projected oil revenues are estimated using the authorities' forecasting model, which takes specific account of the schedule of oil pick-ups. Considering the exogenous risks posed by changes in the number of shipments (including the effect of the minimum volume required to make up a shipment), the quarterly revenue projections for 2006 are based on the following shipment schedule:

Table 1. Government Oil Shipments, 2006

(Number of shipments)[1/]

Product/Blend	2006 Q1	Q2	Q3	Q4
Djéno	7	5	5	5
Nkossa	5	6	7	6
Yombo	0	1	0	0
Butane	1	4	3	3
Propane	0	1	1	1

1/ with a lag of one month.

9. The tax revenue projections take account of the usual one-month lag between the date of shipment and the date of receipt of the sale proceeds by the Treasury. To ensure effective monitoring of oil revenues, the authorities will provide to IMF staff a detailed monthly table of actual shipments within 30 days of the end of the month in which the shipment was made. At a minimum, this table will contain, for each shipment, information on the type of product, the date of loading, the recipient, and the selling price (in US$).

10. Expenditure is measured on a payments order basis. It includes current expenditure, domestically financed capital expenditure, externally financed capital expenditure, and net lending. Current expenditure is defined as total expenditure minus capital expenditure minus net lending. Current expenditure is broken down into personnel expenditure, expenditure on goods and services, interest on the debt (domestic and external), transfers and subsidies, and other current expenditures.

C. Change in the Net Claims of the Banking System on the Central Government

11. The net government position vis-à-vis the banking system (excluding net IMF credit) is defined as the government's claims on domestic banking institutions minus the government's debts to domestic banking institutions. The claims of the government include the cash balances of the Treasury held in the banking system, government deposits at the Bank of Central African States (BEAC), government deposits at commercial banks, and government deposits at the Caisse Nationale d'Épargne (CNE) and the Centre des Chèques Postaux (CCP). Government debts to the banking system include BEAC lending (including statutory advances and consolidated advances), lending to the government by commercial banks (including government securities held by the commercial banks), and CNE/CCP deposits held by the government.

12. The end-of-period stock of net bank claims on the government, excluding the counterpart of the use of Fund resources, is valued in accordance with the accounting framework currently used by the BEAC. On December 31, 2005, these claims amounted to CFAF -76 billion.

D. Debt and External Arrears

13. The definition of government used for the various external debt performance criteria includes government, as defined in paragraph 4, public institutions of an administrative nature (Etablissements Publics Administratifs), public institutions of a scientific and/or technical nature, public institutions of a professional nature, public institutions of an industrial and/or commercial nature (Entreprises Publiques d'Intérêt Commercial), and local governments, with the sole exception of the national oil company (SNPC)—see paragraph 16 below.

14. For the purposes of this memorandum, "debt" and "concessional loans" are defined as follows:

a. As specified in the guidelines adopted by the Executive Board of the IMF,[1] debt will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. The debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement, excluding those payments that cover the operation, repair, or maintenance of the property. Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt.

[1] See Executive Board Decision No. 6230-(79/140) as amended by Decisions Nos. 11096-(95/100) and 12274-(00/85).

Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

b. Loan concessionality is assessed on the basis of the commercial interest reference rates (CIRRs) established by the OECD. A loan is said to be on concessional terms if, on the date of conclusion of the contract, the ratio of the net present value of the loan, calculated on the basis of the reference interest rates, to its nominal value is less than 50 percent (i.e., a grant element of at least 50 percent). For debts with a maturity exceeding 15 years, the ten-year reference interest rate published by the OECD is used to calculate the grant element. For shorter maturities, the six-month market reference rate is used.

15. The quantitative performance criteria with respect to external debt apply not only to debt as defined in the above-mentioned guidelines, but also to commitments incurred or guaranteed for which no value has yet been received or on which only partial drawings have been made. However, this does not apply to financing from the IMF or to Treasury bills and bonds issued by the Congolese Treasury in CFA francs on the CEMAC regional market.

16. For external debt with an initial maturity of less than one year, normal short-term import and export credit are excluded from the scope of the indicator, including the prepayments defined in paragraph 19 below.

17. The ceiling on any new nonconcessional external debt with a maturity of more than one year incurred or guaranteed by the SNPC, with or without government guarantee, will be monitored continuously. The SNPC may borrow only to finance investments related to its core activities (research, exploration, production, refining and distribution of oil, construction of a Brazzaville headquarters, creation and strengthening of its database, etc.). In addition, these investments must be included in the investment program approved by the government. The ceiling on debt does not apply to changes in loan accounts with oilfield partners or to loans of less than one year for operating purposes.

18. The accumulation by the government of external payment arrears is the difference between (a) the gross amount of external debt service payments due (principal and interest, including penalty and/or late interest, as appropriate) and (b) the amount actually paid during the period under consideration. Under the program, the government commits itself to not accumulate external payment arrears on non-reschedulable debt (that is post-cutoff-date debt to Paris Club creditors and debt owed to multilateral creditors). Nonaccumulation of external payment arrears is a criterion to be continuously observed.

E. Oil-Collateralized External Debt

19. Oil-collateralized external debt is external debt that is contracted by giving an interest in oil. Prefinancing is defined as an oil-collateralized loan which is repaid by the sale of the oil in a different calendar year. New prefinancing by or on behalf of the government is strictly prohibited under the program. The refinancing and/or deferral of

the existing stock and/or due dates are permitted but should not give rise to an augmentation of the existing stock of oil-collateralized debt.

20. A prepayment is defined as an advance payment by the purchaser of oil on a specific oil shipment. Prepayment-related operations must be repaid within 6 months but in any case within the calendar year in which they were contracted.

21. The government’s commitment not to contract new oil-collateralized debt will be monitored using the list of oil-collateralized debt as of December 31, 2005, as shown in Annex I.

F. Arrears and Domestic Debt

22. Domestic payment arrears of the government are equivalent to the difference over the relevant period between the amount of payments authorized and the actual payments made (within 90 days). A net reduction in arrears is reflected in the TOFE as a negative amount, and a net accumulation as a positive sum. Payments made by the government cover payments by the Treasury and the CCA, including through clearing operations.

23. The amount of outstanding domestic payment arrears, usually referred to as the “float” in the budget execution tables, particularly the TOFE, will be capped at CFAF 18 billion at the end of each quarter, with the obligation of clearing the float at the end of the year.

VII. ADJUSTMENTS

24. The criterion on the basic primary fiscal balance (paragraph 2.a) will be adjusted upward if oil revenues are higher than projected. Oil revenues will be adjusted in two stages: the first adjustment will take account of the change in the number of shipments, while the second will reflect the change in international oil prices. First, expected oil revenues from the sale of government oil by the SNPC, estimated on the basis of the shipment schedule, will be adjusted by the ratio of the actual number of shipments to the projected number. The adjustment will be calculated separately for each component of government oil revenues generated by shipments sold by the SNPC, for each type of Congolese oil product, namely, the three crude oil blends (Djéno, Nkossa, and Yombo), as well as butane and propane. Secondly, expected oil revenue adjusted by quantity will be multiplied by the ratio of the international price to the projection price. In accordance with the fiscal rule on oil prices, government oil revenues will be projected on the basis of the oil price estimates in the IMF’s *WEO* less a ’prudence’ factor (US$10/barrel beginning in 2006); the price resulting from this calculation will be known as the “estimated adjusted international price.” Consequently, the adjustment of revenues based on price will consist of multiplying total government revenues by the ratio of the international price received to the estimated adjusted international price, calculated in CFA francs. Both adjustments will be made quarterly.

25. The target on the basic primary fiscal balance will be adjusted downward by up to CFAF 50 billion for priority investment projects during the second half of 2006. The adjuster therefore applies only to the quantitative target for end-September 2006, if

domestically-financed capital expenditures as defined in the TOFE exceed CFAF 196 billion at that time, and the performance criterion for end-December 2006, if domestically-financed capital expenditures as defined in the TOFE exceed CFAF 216 billion at that time. These projects will be approved by World Bank staff, would be awarded through transparent and competitive procurement procedures, and approved through a supplementary budget.

26. During the program period (April 1, 2006 to December 31, 2006), if the primary budget surplus exceeds the quantitative program indicator (2a) and/or if additional nonearmarked budgetary support,[2] over and above the programmed amount, becomes available, the government intends to use one-third of these extra resources to further reduce external payment arrears on government debt not eligible for rescheduling. This will be implemented four weeks after the end of the quarter, in consultation with Fund staff. Any remaining additional resources will be deposited in the banking system, and their use will be discussed with IMF staff in the context of program execution reviews. Priority in the use of the additional resources will be given to:

- reduction of the government's priority domestic arrears (wages, benefits of former workers of liquidated enterprises, pensions, and small and medium-sized enterprises) as detailed in a list of creditors;
- reduction of the net claims of the banking system on the government (excluding the counterpart of the use of Fund resources); and/or
- an increase in poverty reduction expenditures.

27. The ceiling on the change in the banking system's net claims on the government will be adjusted if external budgetary support exceeds or falls short of program projections. The ceiling will be adjusted downward by the amount of budgetary support received in excess of the programmed amount. Conversely, the ceiling will be adjusted upward by the amount of the shortfall in budgetary support programmed for the period. This adjustment cannot exceed CFAF 5 billion, calculated on a cumulative basis, during the first year of the program.

VIII. Structural Measures

28. The structural measures are listed in Table 4 of the Memorandum on Economic and Financial Policies.

29. All government revenue and the execution of all government payments will be done through the Treasury. All government revenue must be transferred to the Treasury

[2] Budgetary support is defined as the amount of nonproject grants and loans (excluding IMF resources).

or, in the case of earmarked revenue (intended for various funds and other agencies), transferred to the special earmarked accounts of the Treasury, in accordance with fiscal procedures. All government payments must be made through the Treasury. This provision facilitates budget execution and control.

30. A diagnostic study of the economic viability of the Congolaise de raffinerie (CORAF) will be carried out by an audit firm selected through an international bidding process. The terms of reference and specifications for this study will be reviewed by the staff of the IMF and found satisfactory. The final audit report will be submitted to the Ministry of Finance no later than October 31, 2006.

31. The government will also adopt, by end-September 2006, a timetable for the elimination of all implicit subsidies for refined petroleum products within one year so as to limit the cost to future budget of losses in this sector.

32. External audits of cost oil for 2004 and 2005 as defined in production-sharing contracts (PSCs), reported by oil companies will be carried out in accordance with international audit standards by firms of international reputation. The audits will cover all PSCs, namely: for the operator Total E&P Congo, the PSCs of Haute Mer, Mer Très Profonde Sud, PEX, and PNGF; for the operator Likouala S.A., the Likouala and Likouala-Est concessions; for the operator CongoRep, the Émeraude concession; for the operator ENI Congo, the PSCs of Marine VI, Marine VII, Marine X, Madingo, and Mer Très Profond Nord; and for the operator Zetah M & P Congo, the PSCs of Kouilou and Kouakouala. The audit reports will be submitted to the government no later than December 31, 2006.

33. The quarterly certification of oil revenues by an external auditor, based on the terms of reference used for the 2003 certification and without qualification on access to information, will continue. The certification reports will include, among other things: (i) verification of the tax returns of the oil companies, (including compliance with the terms of PSCs), (ii) reconciliation of the commercial transactions of the SNPC and the quantity of oil due to the government in settlement of the oil companies' tax liabilities (the SNPC included), and (iii) verification that the corresponding revenue has been transferred to the Treasury. The certification report will be available at the latest one quarter after the end of the quarter in question and will be published on the official website of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).

34. An audit firm of international reputation will also be commissioned to carry out a reconciliation report on the amount of oil revenues deposited in government bank accounts, as reported in the quarterly certification reports, and the total oil revenues reported in the government financial operations tables (TOFEs) for each quarter of 2005 and for the year as a whole. The auditors will have full access to all the information needed to carry out this reconciliation exercise in compliance with their terms of reference. The reconciliation report will be submitted to the government and published on the official website of the Ministry of Economy, Finance, and Budget.

35. The external audit of the 2004 consolidated accounts of the SNPC will be based on the terms of reference and specifications used for the 1999-2003 audit. Accordingly,

the tasks of the auditor will be to audit the consolidated financial statements of the parent company and its subsidiaries and to review financial flows, the execution of the management contract, and internal controls. The auditors will submit their final report to the government by end-June 2006, and this report will be published on the official website of the Ministry of Economy, Finance, and Budget.

36. An independent firm of international reputation will be hired to do a diagnostic study of the SNPC's marketing strategy for the sale of government oil. This study will be completed and submitted to the government by end-August 2006. This will be followed by the adoption by the government and SNPC management of an action plan to bring the marketing of government oil up to international standards, at the latest by December 31, 2006.

37. In line with the commitment to improve transparency in the oil sector, the government will publish, on the official website of the Ministry of Economy, Finance, and Budget, a certification report by the *Cour de Comptes* that all public officials (both in the government and at public enterprises) are not personally benefiting from government oil sales by the SNPC or its subsidiaries. This will be done at the latest by June 30, 2006. The government will also publish on this website the full audit report of the awarding in 2005 of the Marine XI oil field concession by end-September 2006.

38. An anti-corruption committee will be established by end-September 2006, whose terms of reference and composition will be satisfactory to IDA and IMF staffs. Following the creation of the committee, a draft anti-corruption law will be submitted to Parliament by December 31, 2006. The law will include, among other things, conflict-of-interest and financial disclosure rules for public officials. These rules will require that all senior public officials (including in the government, civil service, and public enterprises) disclose their wealth and origins of their incomes when acceding to the post and on an annual basis thereafter. The annual disclosure statements are to be declared to the *Cour des Comptes* and certified by the national anti-corruption committee. This committee will publish a summary report on its findings within six weeks of the end of the calendar year.

IX. Information for Program Monitoring

The government will submit the following information to the staff of the International Monetary Fund through its Resident Representative, and within the time period specified below.

A. Oil Sector

39. The government will submit the following information to the staff of the International Monetary Fund:

- monthly data on oil production by oil field, production costs, volume exported, export prices, and the operations of the Société nationale des pétroles du Congo (SNPC);

- the breakdown of the share of crude oil that accrues to the government, by oil well, distinguishing the type of taxation to which this share relates (royalties, profit oil, etc.);

- any change in the tax parameters; and

- a breakdown of oil prices.

40. Oil prepayments (see paragraph 18 above) are recorded in the TOFE accounts as follows:

- At the time the prepayment is cashed, the amounts received are recorded as debt; the amounts corresponding to commissions paid out are recorded as current expenditure.

- The prepayment is repaid with the proceeds of the sale of oil; at the time of the repayment transaction, the revenue derived from the sale of oil is recorded as final oil revenue accruing to the Treasury, and the amount of the repayment is posted as negative financing (repayment).

B. Government Finance

41. The government will submit the following information to the staff of the International Monetary Fund:

- A table on government fiscal operations (TOFE) and its annexes. The annexed tables include the breakdown of oil revenue in value terms with the corresponding notes on computation, excess oil trends and any bonus payments, the breakdown of tax and nontax revenue, and the breakdown of central government expenditure, particularly transfers and common expenses. The provisional TOFE and its annexes will be reported monthly within four weeks of the end of the month, whereas the final TOFE and its annexes will be reported within six weeks of the end of each month;

- Monthly data on the prices and taxation of petroleum products. These data will include: (i) the price structure in effect during the month; (ii) the details of computation of the price structure, (f.o.b. Mediterranean price) at retail prices; (iii) amounts released for sale; and (iv) a breakdown of the tax revenue from oil products—customs duties and value-added tax—and direct/indirect subsidies supported by the budget. These data will be reported within four weeks of the end of the month;

- Data on implementation of the public investment program, including the breakdown of financing sources. If the data on the execution of investments financed with foreign grants and loans are not available on schedule, a linear estimate of execution in comparison with annual forecasts will be used. These data will be reported on a quarterly basis within four weeks of the end of the quarter; and

- Complete monthly data on nonbank domestic financing of the budget (net bank credit to, and net nonbank funding of, the government). These data will be reported monthly within four weeks of the end of the month.

- The table used to monitor the expenditure process will list the amount of commitments, payment orders, and payments, for both operating and capital expenditures. It will be produced on a quarterly basis, and submitted to Fund staff no later than four weeks after the end of the quarter.

- Pending finalization of the functional classification of government expenditures, the government will prepare and submit to the IMF a quarterly table for monitoring poverty reduction expenditures, based on the pro-poor sectors as defined in the I-PRSP (basic health care and education; infrastructure and rural integration; water and electricity; disarmament, demobilization and reinsertion; social protection, and agriculture). The quarterly tables will be submitted no later than four weeks after the end of the quarter.

C. Monetary Sector

42. The government will submit on a monthly basis, within four weeks of the end of the month, the following preliminary information:

- data on net bank credit to the government;

- the consolidated balance sheet of the monetary institutions, the central bank survey, and the survey of commercial banks;

- the integrated monetary survey;

- lending and deposit rates; and

- the usual banking supervision indicators for banks and nonbank financial institutions, where necessary.

The final data on the integrated monetary survey will be provided within six weeks of the end of the month.

D. Balance of Payments

43. The government will submit the following to the staff of the International Monetary Fund:

- any revised balance of payments data (including services, private transfers, official transfers, and capital transactions) as soon as the data are revised;

- foreign trade statistics (volume and price) prepared by the national statistics agency/BEAC, within three months of the end of the reporting month; and

- the preliminary annual balance of payments data, within nine months of the end of the reference year.

E. Debt

44. The government will submit the following to the staff of the IMF within four weeks of the end of the month:

- data on the stock, accumulation, and payment of domestic arrears;
- data on the stock, accumulation, and payment of external payment arrears;
- a breakdown of estimated domestic and external public debt service, service due, and actual payments, including breakdowns of principal and interest and by creditor;
- the list and amounts of new external debt incurred or guaranteed by the government, with detailed information on the terms and conditions (currency, interest rate, grace period, and maturity) stated in the original agreement; and
- actual disbursements of foreign financial assistance (project and nonproject), including new borrowing and any external debt relief granted by foreign creditors (CCA tables).

F. Real Sector

45. The government will submit the following to the staff of the IMF:

- monthly itemized consumer price indices, within four weeks of the end of the month;
- provisional national accounts, within nine months of the end of the year;
- any revision of the national accounts; and
- any other indicators and statistical data used to track overall economic developments, including information on activity in the forestry sector and wood-processing industry, as well as the short-term economic bulletins prepared monthly.

G. Structural Reforms and Other Information

46. The government will submit the following information:

- any study or official report on the economy of the Republic of Congo, within two weeks of its publication; and

- any decision, order, law, decree, ordinance, or circular having economic or financial implications, within two weeks from the time it is published, or, at the latest, from its entry into force.

Stock of Oil-Collateralized Debt as of December 31, 2005[3]

Description	Total stock (millions of CFA francs)
TEP Congo	5.4
ChevronTexaco (Etat1)	8.9
Central a Gaz (AGIP)	0
RMB-VITOL	21.4
BNP/BPPB	28
ChevronTexaco (Etat2)	7.2
Total collateralized debt	74.9

[3] Excluding arrears under litigation to one creditor.